Supreme Court, U.S.
FILED

(1) 96 153 JUL 29 1996

No. OFFICE OF THE CLERK

In The

Supreme Court of the United States

October Term, 1995

THE SCOTTISH HERITABLE TRUST, PLC and SHT HOLDINGS (US), INC.,

Petitioners,

vs.

PEAT MARWICK MAIN & CO. and KPMG PEAT MARWICK,

Respondents.

Petition for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

PETITION FOR A WRIT OF CERTIORARI

DALE A. COOTER
Counsel of Record
JAMES E. TOMPERT
COOTER, MANGOLD, TOMPERT & CHAPMAN, P.L.L.C.
Attorneys for Petitioners
815 Connecticut Avenue, N.W.
Suite 301
Washington, D.C. 20006
(202) 289-5600

9191
Lutz Appellate Services, Inc.
(800) 3 APPEAL • (800) 5 APPEAL • (800) BRIEF 21

43 pp

QUESTIONS PRESENTED

1. Whether the 1991 Amendment to Fed. R. Civ. P. 50(a) alters the result in those cases in which courts have used various techniques to avoid the requirement that a motion for judgment at the close of the evidence be made as a predicate to a motion for judgment notwithstanding the verdict?

2. Whether an "*Erie* guess" by a United States Court of Appeals can ignore an interpretation of state law by intermediate appellate courts of the forum State, where there is no persuasive data to the contrary?

PARTIES TO THE PROCEEDINGS

The Scottish Heritable Trust, PLC and SHT Holdings (US), Inc., were the Plaintiffs in the District Court and the Appellees and Cross-Appellants in the Court of Appeals.

Peat Marwick Main & Co. and its successor by name change, KPMG Peat Marwick, were the Defendants in the District Court and the Appellants and Cross-Appellees in the Court of Appeals. Those entities are now known as KPMG Peat Marwick LLP.

The Scottish Heritable Trust, PLC and SHT Holdings (US), Inc. respectfully petition for a writ of certiorari to review the judgment of the United States Court of Appeals for the Fifth Circuit in this case.

TABLE OF CONTENTS

	Page
Questions Presented	i
Parties to the Proceedings	ii
Table of Contents	iii
Table of Citations	iv
Opinions Below	1
Statement of Jurisdiction	1
Statutory Provisions Involved	1
Statement of the Case	1
Reasons for Granting the Writ	6
I. There Is An Important Question Of Federal Law Whether The 1991 Amendment to Fed. R. Civ. P. 50(a) Alters Prior Case Law, That Has Not Been, But Should Be Decided By This Court.	7
II. The Decision Of The Fifth Circuit Is In Conflict With Decisions Of Other Courts Of Appeals On The Same Important Issue.	15
III. The Fifth Circuit's Application Of Law Is In Violation Of *Erie* And In Conflict With Opinions Of The Fifth And Other Circuits.	20

Contents

Page

A. Texas State Law 21

B. The Fifth Circuit *Erie* Guess 26

Conclusion 30

TABLE OF CITATIONS

Cases Cited:

Albrecht v. Herald Co., 425 F.2d 124 (8th Cir. 1970), *cert. denied*, 400 U.S. 866 (1971) 19

American Protein Corp. v. AB Volvo, 844 F.2d 56 (2d Cir.), *cert. denied*, 488 U.S. 852 (1988) 19

Benson v. Allphin, 786 F.2d 268 (7th Cir.), *cert. denied*, 479 U.S. 848 (1986) 17

Blue Bell, Inc. v. Peat, Marwick, Mitchell & Co., 715 S.W. 2d 408 (Tex. Civ. App. - Dallas 1986, writ ref'd n.r.e.) 20, 22, 23, 24, 25, 26, 29, 30

Borse v. Pierce Goods Shop, Inc., 963 F.2d 611 (3d Cir. 1992) 21

Boynton v. TRW, Inc., 858 F.2d 1178 (6th Cir. 1988) ... 19

Catlett v. Local 7370 of United Paper Workers, 69 F.3d 254 (8th Cir. 1995) 14

Comer v. Texaco Inc., 514 F.2d 1243 (5th Cir. 1975) ... 29

Contents

Page

Cook Consultants, Inc. v. Larson, 700 S.W. 2d 231 (Tex. Civ. App.-Dallas 1985, writ ref'd n.r.e.) 20, 22, 23, 24, 26, 28

Cross v. Cummins Engine Co., 993 F.2d 112 (5th Cir. 1995) 21

De Marines v. KLM Royal Dutch Airlines, 580 F.2d 1193 (3d Cir. 1978) 19

Downes v. Volkswagen of America, Inc., 41 F.3d 1132 (7th Cir. 1994) 15, 16

Eastern Mountain Platform Tennis, Inc. v. Sherwin Williams Co., 40 F.3d 492 (1st Cir. 1994) 21

Farley Transp. Co. v. Santa Fe Transp. Co., 786 F.2d 1342 (9th Cir. 1985) 18

Faveline. Inv., S.A. v. Municipality of Ponce, 645 F.2d 92 (1st Cir. 1981) 19

Fidelity Union Trust v. Field, 311 U.S. 169 (1940) 21

Hermann Hosp. v. National Standards Ins. Co., 776 S.W. 2d 249 (Tex. Civ. App.-Houston 1989, writ denied) 20, 24, 25, 26, 28, 29

Hilard Chemical Corp. v. Ricoh Electronics, Inc., 875 F.2d 32 (2d Cir. 1989) 12

Contents

Page

In re Crazy Eddie Securities Litigation, 812 F. Supp. 357 (E.D.N.Y. 1993) 6, 20, 26, 27, 28, 29

In re: Owners of Harvey Oil Center, 788 F.2d 275 (5th Cir. 1986) 12

Jackson v. City of Cookeville, 31 F.3d 1354 (6th Cir. 1994) 17

Lewis v. Kendrick, 944 F.2d 949 (1st Cir. 1991) 19, 20

Libbey-Owens-Ford v. Insurance Co. of N. America, 9 F.3d 422 (6th Cir. 1993) 13

Lifshitz v. Walter Drake & Sons, 806 F.2d 1426 (9th Cir. 1986) 19

Little v. Bankers Life & Cas. Co., 426 F.2d 509 (5th Cir. 1970) 12

Lowenstein v. Pepsi-Cola Bottling Co. of Pennsauken, 536 F.2d 9 (3d Cir.), *cert. denied*, 429 U.S. 966 (1976) 20

Mallick v. International Broth. of Elec. Workers, 644 F.2d 228 (3d Cir. 1981) 13, 20

McArthur v. University of Tex. Health Center Tyler, 45 F.3d 890 (5th Cir. 1995) 15

Montgomery Ward & Co. v. Duncan, 311 U.S. 243 (1940) 14

Contents

Page

Moran v. Raymond, 484 F.2d 1008 (7th Cir. 1973), *cert. denied*, 415 U.S. 932 (1974) 18

Mosley v. Cia. Adra. S.A., 362 F.2d 118 (2d Cir.), *cert. denied*, 383 U.S. 933 (1966) 18

Ohler v. Trinity Portland Cement Co., 181 S.W.2d 120 Tex. Civ. App. - Galveston 1994) 29, 30

Puckett v. Tennessee Eastman Co., 889 F.2d 1481 (6th Cir. 1989) 21

Pulla v. Amoco Oil Co., 882 F. Supp. 836 (S.D. Iowa 1994), *affirmed in part, reversed in part on other grounds*, 72 F.3d 648 (8th Cir. 1995) 14, 18

Purcell v. Sequin State Bank & Trust Co., 999 F.2d 950 (5th Cir. 1993) 19

Quinn v. Southwest Wood Products, Inc., 597 F.2d 1018 (5th Cir. 1979) 12

Shatterproof Glass Corp. v. James, 466 S.W. 2d 873 (Tex. Civ. App.-Ft. Worth 1971, writ ref'd. n.r.e.) 20, 21, 22, 23, 25

Six Cos. of California v. Joint Highway Dist. No. 13, 311 U.S. 180 (1940) 21

Steiner v. Southmark Corp., 734 F. Supp. 269 (N.D. Tex. 1990) 24, 25, 29

Contents

Page

Steiner v. Southmark Corp., 739 F. Supp. 1087 (N.D. Tex. 1990) 25, 26, 29

Stoner v. New York Life, 311 U.S. 464 (1940) 20, 21

Trujillo v. Goodman, 825 F.2d 1453 (10th Cir. 1987) ... 18

Umplehy v. Potter & Bromfield, 69 F.3d 209 (7th Cir. 1995) 16

United States v. Spaddiccino, 800 F.2d 292 (2d Cir. 1986) 21

U.S.E.E.O.C. v. AIC Security Investigations, LTD, 55 F.3d 1276 (7th Cir. 1995) 17

Warlick v. Cross, 969 F.2d 303 (7th Cir. 1992) 16

West v. American Tel. & Tel. Co., 311 U.S. 223 (1940) .. 21

Whelan v. Abell, 48 F.3d 1247 (D.C. Cir. 1995) 18

Yohannon v. Keene Corp., 924 F.2d 1255 (3d Cir. 1991) 14

Statutes Cited:

28 U.S.C. § 1254(1) 1

Contents

Page

Federal Rules of Civil Procedure:

Rule 50(a) ..... i, 1, 5, 6, 7, 8, 10, 15, 18, 19

Rule 50(a)(1) 10

Rule 50(a)(2) 6, 9, 10, 11, 13, 15, 16, 17, 18, 20

Rule 50(b) 12, 19

United States Constitution Cited:

Seventh Amendment 7, 13, 14

Other Authorities Cited:

C. Wright, A. Miller & E. Cooper, *Federal Practice and Procedure* § 4507 (1996) 21

Moore's Federal Practice 1996 Rules Pamphlet ¶ 50.4 (1996) 16

Restatement (Second), Torts § 552 ...21, 22, 23, 24, 25, 26, 29

APPENDIX

Appendix A — Opinion of the United States Court of Appeals for the Fifth Circuit Dated April 30, 1996 ..... 1a

Contents

Page

Appendix B — Order of the United States District Court for the Northern District of Texas, Dallas Division Filed September 26, 1994 ..... 24a

Appendix C — Second Amended Final Judgment of the United States District Court for the Northern District of Texas, Dallas Division Filed September 26, 1994 ... 30a

Appendix D — Relevant Statutes 32a

OPINIONS BELOW

The opinion of the United States Court of Appeals for the Fifth Circuit (App. *infra*, 18a-31a) is reported at 81 F.3d 606 (5th Cir. 1996).

STATEMENT OF JURISDICTION

The judgment of the Court of Appeals was entered on April 30, 1996. The jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

The 1991 Amendment to Rule 50(a) of the Federal Rules of Civil Procedure is reproduced in Appendix D (32a-33a).

STATEMENT OF THE CASE[1]

This dispute concerns the purchase of the Rangaire Corporation ("Rangaire") by Plaintiff Scottish Heritable, Inc. ("SHT(US)") a wholly owned subsidiary of Plaintiff Scottish Heritable Trust, PLC ("SHT/PLC") (collectively "SHT"), a public company in the United Kingdom. As explained below, SHT purchased Rangaire in reliance upon financial statements certified by Defendant Peat Marwick Main & Co. and its successor by name change, Defendant KPMG Peat Marwick ("Peat") in which Rangaire's net worth was overstated by approximately 50%.

---

1. Since this Petition presents two distinct questions for review, one procedural concerning the scope of the 1991 Amendment to Rule 50(a) of the Federal Rules of Civil Procedure and one substantive concerning the "*Erie* guess" of Texas law by the Court of Appeals, both the facts and procedure material to the consideration of the questions presented are set forth herein.

Rangaire was a public company based in Cleburne, Texas whose stock was traded on the National Association of Securities Dealers Automated Quotation System (NASDAQ). The company's primary line of business was the production of lime.

From 1962 until 1990, Rangaire's financial statements were audited by Peat Marwick. Joseph "Mac" Hill ("Hill") worked as an accountant for Peat from 1958 until 1962, when he left to join Rangaire as its Comptroller. Thereafter, Hill exercised complete domination of all the Rangaire accounting systems and personally determined the accounting treatment of all fixed assets. Hill continued to personally determine the treatment of individual assets on the books even after his promotion to the position of President and Chief Operating Officer in 1973 until his resignation in 1990.

At least as early as 1983, Hill and Peat Marwick knew that Eugene Roberts ("Roberts"), Rangaire's founder and Chairman, was in financial difficulty and wanted to sell his 28% stock interest in Rangaire. In 1985, Rangaire retained an investment banker to sell "all or a portion" of the company. The search for a buyer was well known to Peat Marwick. Although Rangaire could not find a buyer in 1985-1986 it remained on the market for sale and "major players" in the lime business visited the company in connection with a possible purchaser. The ultimate buyer of control of Rangaire was SHT(US).

Apparently beginning in 1985, Hill undertook a series of actions to "cook the books" of Rangaire. He artificially inflated the assets of the company on its balance sheet each year until the company was acquired, thereby artificially increasing the value of Rangaire stock owned by both he and Roberts. These actions included the wholesale extension of the useful lives of fixed assets on the books in 1985, the improper capitalization of repairs, the continuation of assets on the books after they either ceased to exist or had been abandoned, and the capitalization of

small assets normally expensed. These actions resulted in published financial statements showing a profitable company with a strong underlying portfolio of fixed assets in each year from 1985 through 1988. Each year-end statement followed an audit by Peat Marwick and contained a certification by Peat Marwick that the audits had been conducted in conformance with Generally Accepted Auditing Standards ("GAAS") and that the statements "present fairly" the financial condition of the company.

In reality the company was at best marginally profitable and the fixed assets were non-existent, abandoned or in disrepair. There was testimony that the fixed assets in the lime plants were obsolete, "everything was junk," held together with "bailing wire and bubble gum," and that a lot of equipment with high book value was not worth anything. For instance, in a test count of parts inventory by a Peat auditor, out of the total 60 items selected 30 did not exist and additionally 20 counts were incorrect.

Roberts filed for bankruptcy in December 1987. Resultantly, Rangaire retained an investment banker to arrange for a sale of, at the very least, the Roberts stock. Peat Marwick knew that the audited statements would be relied upon by the investing public in a purchase of the Roberts stock. Because Rangaire was a public company, potential buyers were limited to information in the public domain.

Introduced to the company by its investment advisor, SHT analyzed the available public material and its representatives met with Hill to discuss a purchase of control. In reliance upon the Peat Marwick certification of the financial statements, on August 8, 1988, SHT purchased the Roberts stock from the bankruptcy trustee. Soon after this purchase, SHT became dissatisfied with Hill. To be in full control, and consistent with its original intent, during the period of time September through

December 1988, SHT purchased additional Rangaire stock, bringing its total stake in the company to approximately 50%, at a total investment price of approximately $15,300,000. In making these purchases SHT again relied on the financial statements audited by Peat Marwick.

In the Summer of 1989, SHT learned of some of the accounting irregularities mentioned above. An investigation began in conjunction with the 1989 audit by Peat Marwick. Although it took some time for the magnitude of the problem to surface, the ultimate result was that Rangaire was forced to write off approximately 50% of its net worth.

A dispute arose between SHT and Peat Marwick, as to the reason for the write-off. SHT contended that the write-off was the result of accounting errors by Peat Marwick, while Peat Marwick contended that the write-off was the result of events occurring in 1989.

The result of the write-off was catastrophic. Within a year after announcement, the value of the SHT stock had declined by $7,770,524. There was an additional loss to SHT of approximately $5,000,000 incurred in trying to work out of the Rangaire investment.

The action in the District Court ensued. On July 13, 1990, SHT filed its Complaint against Peat Marwick for security law violations, negligent misrepresentation and other claims. On November 12, 1993, the case proceeded to a jury trial in the District Court which lasted approximately five weeks. At the conclusion of SHT's case, Peat Marwick made an oral motion for judgment on certain issues, which was denied. At the close of all the evidence Peat Marwick did not make a motion for judgment. Instead, immediately before closing argument, Peat Marwick objected to some of the jury instructions.

The case was submitted to the jury on SHT's claims of securities law violations and negligent misrepresentation. The jury determined that Peat Marwick was not liable for the securities law violations. On the negligent misrepresentation claim, however, the jury returned a verdict in favor of SHT and awarded $8,500,000 in compensatory damages.

Peat Marwick then filed a Motion for Judgment Notwithstanding the Verdict, or in the Alternative for New Trial. SHT filed a Motion to Strike Peat Marwick's Motion for Judgment Notwithstanding the Verdict on grounds that Peat did not make a motion for judgment at the close of all the evidence as required by Rule 50(a) of the Federal Rules of Civil Procedure.

The District Court denied both Peat Marwick's Motion for New Trial and SHT's Motion to Strike. The District Court concluded that SHT had a claim for negligent misrepresentation under Texas law. The District Court granted, in part, Peat's Motion for Judgment Notwithstanding the Verdict and reduced the judgment to $4,725,000 on grounds that there was insufficient evidence to support some of the damages awarded by the jury.

On October 12, 1994, Peat Marwick filed a Notice of Appeal to the United States Court of Appeals for the Fifth Circuit and on October 18, 1994, SHT filed a Notice of Cross Appeal. On appeal, SHT raised the issue that Peat Marwick waived its right to challenge the sufficiency of the evidence because it failed to make a motion for judgment at the close of the evidence as required by Rule 50 (a) of the Federal Rules of Civil Procedure. SHT argued extensively that the 1991 Amendment to Rule 50(a) and the Notes of the Advisory Committee mandate a finding of waiver. Peat Marwick's response was that its objections to the jury instructions, under Fifth Circuit case law, were sufficient to preserve the issues it raised on appeal. Peat Marwick also argued that SHT did not have a claim for negligent misrepresentation under Texas law.

On April 30, 1996, the Court of Appeals reversed the District Court's judgment and rendered a "take-nothing judgment in favor of Peat Marwick." App., *infra*, 2a. In pertinent part, the Court of Appeals held that Peat Marwick did not waive its right to challenge the sufficiency of the evidence on appeal because it failed to move for judgment at the close of all the evidence. *Id.* at 9a. The Court held that "we liberally construes [sic] Rule 50(b) of the Federal Rules of Civil Procedure" and opined that Peat's objections to the jury instructions were sufficient to preserve the issues it raises on appeal. *Id.* at 9a-10a. The Court also made "an *Erie* guess as to how the Texas courts would come down on" the issue of what constitutes a limited class in a claim of negligent misrepresentation under Texas law. *Id.* at 17a. The Court relied upon an opinion by the United States District Court for the Eastern District of New York in *In re Crazy Eddie*, 812 F. Supp. 338, 357 (E.D.N.Y. 1993) and concluded that SHT did not have a claim of negligent misrepresentation under Texas law. *Id.* at 16a-20a, 23a.

REASONS FOR GRANTING THE WRIT

There is an important question of federal law whether the 1991 Amendment to Rule 50(a) of the Federal Rules of Civil Procedure alters the result in those cases in which courts have used various techniques to avoid the requirement that a motion for judgment at the close of the evidence be made as a predicate to a motion for judgment notwithstanding the verdict. In this case, the Fifth Circuit ignored the express language of Rule 50(a)(2) and the Notes of the Advisory Committee, and decided that the 1991 Amendment does not alter prior case law. App. 9a-10a.

The question of whether the 1991 Amendment alters prior case law is an important question, which has not been, but should be decided by this Court. This is an important question because it affects every civil jury trial in the United States District Courts, the vast majority of civil appeals to the United States Courts of

Appeals and the Seventh Amendment right to a trial by jury. There are a wide range of disparate rulings by the Courts of Appeal on this issue. As such, this is an issue which has not been, but should be decided by the Supreme Court.

There is also a conflict between the Circuits on this issue. The Fifth Circuit and other Circuits that liberally construe Rule 50 are in conflict with the Seventh Circuit and the District of Columbia Circuit. The Seventh Circuit has expressly held in a series of recent cases that the 1991 Amendment to Rule 50(a) and the Notes to the Advisory Committee have altered prior exceptions in the case law. There is also a spilt and confusion in the Circuits over the scope of any exceptions to the requirements of Rule 50(a) and whether objections to jury instructions can serve as a substitute for a motion for judgment at the close of the evidence. This is an area of law that is badly in need of this Court's authoritative voice.

Additionally, the Fifth Circuit ignored the clear holdings of four Texas intermediate court cases on the issue of negligent misrepresentation. This failure to abide by the holdings of the Texas courts put the Fifth Circuit in conflict with the decisions of this Court, prior Fifth Circuit precedent, and other Circuits. It is well established that, in the absence of other persuasive data about how a state high court will decide an issue, the federal court, pursuant to *Erie*, is bound by the decision of the intermediate court. Because *Erie* is a critical part of the backbone of the federal system, it is important for this Court to ensure that its dictates are enforced.

I. There Is An Important Question Of Federal Law Whether The 1991 Amendment To Fed. R. Civ. P. 50(a) Alters Prior Case Law, That Has Not Been, But Should Be Decided By This Court.

The Federal Rules of Civil Procedure require that a motion for judgment as a matter of law be made at the close of the

evidence as a predicate to a motion for judgment notwithstanding the verdict. Rule 50 (a) sets forth the procedure for a motion for judgment as a matter of law.

Prior to the 1991 Amendment, Rule 50(a) was just one paragraph which provided:

> (a) Motion for Directed Verdict: When Made; Effect. A party who moves for directed verdict at the close of the evidence offered by an opponent may offer evidence in the event that the motion is not granted, without having reserved the right so to do and to the same extent as if the motion has not been made. A motion for directed verdict which is not granted is not a waiver of trial by jury even though all parties to the action have moved for directed verdicts. A motion for a directed verdict shall state the specific grounds therefor. The order of the court granting a motion for a directed verdict is effective without any assent of the jury.

The 1991 Amendment divided paragraph (a) into two separate paragraphs, (1) and (2) as follows:

> (1) If during a trial by jury a party has been fully heard on an issue and there is no legally sufficient evidentiary basis for a reasonable jury to find for that party on that issue, the court may determine the issue against that party and may grant a motion for judgment as a matter of law against that party with respect to a claim or defense that cannot under the controlling law be maintained or defeated without a favorable finding on that issue.

> (2) Motions for judgment as a matter of law may be made at any time before submission of the case to the jury. Such a motion shall specify the judgment sought and the law and the facts on which the moving party is entitled to the judgment.

For purposes of this petition, the new subparagraph (1) is essentially irrelevant. It merely changed the denomination of a motion for directed verdict to a motion for judgment as a matter of law and articulated the accepted standard in the case law for granting a motion for judgment as a matter of law.

What is critical for purposes of this petition, and for all civil litigators, is the new subparagraph (2), particularly the second sentence of the subparagraph which provides that the "motion *shall specify the judgment sought and the law and the facts on which the moving party is entitled to judgment.*" Fed. R. Civ. P. 50(a)(2) (emphasis supplied). Prior to the 1991 Amendment, the only requirement was that the motion "shall state the specific grounds." As such the 1991 Amendment has expanded the requirement of a party seeking judgment as a matter of law. The moving party can no longer just make a motion which states the specific grounds for relief, but must now do three things in a motion for judgment as a matter of law, namely: (1) specify the judgment sought, (2) specify the facts on which the party seeks judgment and (3) specify the law on which the party seeks judgment.

As such, the 1991 Amendment alters federal law on an important issue. The Amendment no longer allows a party to use various techniques to avoid making a motion for directed verdict as a predicate to a motion for judgment notwithstanding the verdict. For instance, the Amendment makes it impossible for a party to use an objection to a jury instruction as a substitute for a motion for directed verdict, which is precisely what the Court of Appeals allowed in the case below. An objection to another

party's jury instruction is not, and cannot be, a motion for judgment as a matter of law which (1) specifies the judgment sought, (2) specifies the facts on which that party seeks judgment and (3) specifies the law on which that party seeks judgment.[2]

This conclusion is mandated by the Notes of the Advisory Committee for the 1991 Amendment. 28 U.S.C.A. Rule 50, Advisory Committee Notes, 1991 Amendment (1992). The Notes of the Advisory Committee for the 1991 Amendment to subparagraph (a) are extensive and very instructive. At first the Advisory Committee explained the change in the nomenclature of a motion for directed verdict to a motion for judgment as a matter of law, and then explained that paragraph (a)(1) "articulates the standard for the granting of a motion for judgment as a matter of law" which is the same standard accepted in the case law. Advisory Committee Notes, 1991 Amendment.

More significantly is the Advisory Committee's discussion of the addition of subparagraph (a)(2). The Advisory Committee explained that "Paragraph (a)(2) retains the requirement that a motion for judgment be made prior to the close of the trial, subject to renewal after a jury verdict has been rendered." *Id.* The Committee emphasized that "[t]he purpose of this requirement is to assure the responding party an opportunity to cure any deficiency in that party's proof." *Id.* The Committee

---

2. Only if a party were to *offer* a jury instruction which asks the Court for directed verdict, which the Court treats as a motion for judgment, and in the submission of that instruction the party (1) specifies the judgment sought, (2) specifies the facts on which the party seeks judgment and (3) specifies the law on which the party seeks judgment, would the requirements of the 1991 Amendment be satisfied. This is of course, assuming, and giving the party the benefit of the doubt that its failure to call or label such an instruction a motion for judgment as a matter of law, is such technical non-compliance with the rule that it would be excused. It is undisputed that Peat Marwick did not offer any such instruction in this case, instead, at best, Peat Marwick only objected to certain instructions submitted by the District Court.

then explained the significance of the second sentence in paragraph (a)(2):

> The second sentence of paragraph(a)(2) does impose a requirement that the moving party articulate the basis on which a judgment as a matter of law might be rendered. The articulation is necessary to achieve the purpose of the requirement that the motion be made before the case is submitted to the jury, so that the responding party may seek to correct any overlooked deficiencies in the proof. *The revision thus alters the result in cases in which courts have used various techniques to avoid the requirement that a motion for a directed verdict be made as a predicate to a motion for judgment notwithstanding the verdict.* E.g., *Benson v. Allphin,* 788 F.2d 268 (7th Cir.1986) ("this circuit has allowed something less than a formal motion for directed verdict to preserve a party's right to move for judgment notwithstanding the verdict"). *See generally* 9 WRIGHT & MILLER, FEDERAL PRACTICE AND PROCEDURE § 2537 (1971 and Supp.). The information required with the motion may be supplied by explicit reference to materials and argument previously supplied to the court.

Id. (emphasis supplied). Accordingly, the Advisory Committee agrees with the analysis set forth above, and mandates the conclusion that the 1991 Amendment alters the result in cases in which courts have used various techniques, such as objections to jury instructions, to avoid the requirement that a motion for

judgment as a matter of law be made at the close of the evidence.[3]

There are three reasons why the question of whether the 1991 Amendment alters the case law is an important question. First, it is an important question because it affects trial procedure for every civil jury trial in the United States District Courts throughout the country. In every civil jury trial a clear definition of what constitutes the appropriate procedural predicate for a post-trial challenge to the evidence is essential.

Second, the question is an important question because it also

---

3. The significance of a motion for judgment as a matter of law at the close is that pursuant to Rule 50(b) of the Federal Rules of Civil Procedure, it is a predicate for a post-trial motion for judgment as a matter of law. Pursuant to Rule 50(b), it is well settled that if a party fails to move for a judgment as a matter of law at the close of the evidence, then that party has waived any motion for judgment NOV and the sufficiency of the evidence supporting a jury verdict is not reviewable on appeal. *See Quinn v. Southwest Wood Products, Inc.*, 597 F.2d 1018, 1024-1025 (5th Cir. 1979) ("the sufficiency of the evidence supporting a jury verdict is not reviewable on appeal nor may a motion for judgment N.O.V. be granted, unless a motion for directed verdict was made at the close of all the evidence"); *Hilard Chemical Corp. v. Ricoh Electronics, Inc.*, 875 F.2d 32, 37 (2nd Cir. 1989) ("The rule is well established that a motion for directed verdict at the close of all the evidence is a prerequisite for j.n.o.v."); *In re: Owners of Harvey Oil Center*, 788 F.2d 275, 278 (5th Cir. 1986) (failure to move for a directed verdict at the close of plaintiffs' case precluded motion JNOV). In *Quinn*, the United States Court of Appeals for the Fifth Circuit explained the policy behind the rule:

> [A] litigant may not gamble on a jury's verdict and then later question the sufficiency of the evidence on appeal. . . . Similarly, the litigant who has not moved for a directed verdict in the trial court must have been of the view that the evidence made a case for the jury; he should not be permitted on appeal to impute error to the trial judge for sharing that view.

597 F.2d at 1024-1025 (*quoting Little v. Bankers Life & Cas. Co.*, 426 F.2d 509, 511 (5th Cir. 1970)).

affects the vast majority of civil appeals to the United States Courts of Appeals. The first consideration in the vast majority of civil appeals is what issues have been preserved for appeal. The Courts of Appeals devote substantial time and attention in their preliminary determination of what issues have been preserved for appeal.

Third, the question is an important question because it affects a party's right to a trial by jury. The requirement that a motion for judgment at the close of the evidence serves as a predicate for a post-trial motion for judgment is intended to preserve the Seventh Amendment right to a trial by jury. To the extent that the Circuits allow exceptions to the requirement of a motion for judgment at the close of the evidence, then a party's constitutional right to trial by jury is adversely affected. *See Libbey-Owens-Ford v. Insurance Co. of N. America*, 9 F.3d 422, 426 (6th Cir. 1993) (the "waiver rule serves to protect litigants' Seventh Amendment right to a trial by jury"). As the Court explained in *Mallick v. International Broth. of Elec. Workers*, 644 F.2d 228, 233 (3rd Cir. 1981):

> Unless a court has been alerted to deficiencies in proof by a motion for a directed verdict, a request that the court enter a judgment contrary to that of the jury is tantamount to asking the court to re-examine the facts as found by the jury. Such a re-examination would abridge the Seventh Amendment.

In this regard, a close reading of the Notes of the Advisory Committee for the 1991 Amendment shows that the Advisory Committee was especially concerned with fairness and notice to the non-moving party, and cognizant of the Seventh Amendment. It is fundamentally unfair for a party, such as SHT, to have relied upon the express language of Rule 50(a)(2) with

the belief at the close of the evidence that its claim for negligent misrepresentation was not in jeopardy, only to have its $8,500,000 jury verdict set aside and the Court of Appeals render a "take-nothing judgment." As such, SHT's Seventh Amendment right to trial by jury has been completely nullified.

The question of whether the 1991 Amendment alters prior case law is a question that has not been decided by this Court. The last time there was a significant relevant interpretation of Rule 50 by this Court was in 1940 when the Court held that a motion for judgment notwithstanding the verdict can be granted, even though a motion for directed verdict at the close of the evidence was denied. *Montgomery Ward & Co. v. Duncan*, 311 U.S. 243, 250 (1940).

This is an issue which should be decided by this Court. In the present state of the law there is a wide range of disparate rulings by the United States Courts of Appeals. *See Pulla v. Amoco Oil Co.*, 882 F. Supp. 836, 851-856 (S.D. Iowa 1994), *affirmed in part, reversed in part on other grounds*, 72 F.3d 648, (8th Cir. 1995) (the District Court discusses the disparate rulings by the Circuit Courts at length); *see also Catlett v. Local 7370 of United Paper Workers*, 69 F.3d 254, 259 n.6 (8th Cir. 1995) (the Eighth Circuit noted four different exceptions created by the Circuit Courts, *i.e.*, (1) "substantial compliance" exception, (2) manifest injustice exception, (3) where the trial judge "excused the failure to renew" and (4) "the additional evidence was brief and inconsequential"); *Yohannon v. Keene Corp.*, 924 F.2d 1255, 1261-1262 (3d Cir. 1991) (the Third Circuit noted three different exceptions created by the Circuit Courts, *i.e.*, the (1) "manifest injustice" exception, (2) the "no evidence" exception and (3) the "reinterpretation" exception). In order for civil litigants, District Court judges and the various panels of the Courts of Appeals to have a fair understanding of what is required under Rule 50 as a predicate for post-trial review, it is necessary for this Court to clarify the law on this important issue.

II. The Decision Of The Fifth Circuit Is In Conflict With Decisions Of Other Courts Of Appeals On The Same Important Issue.

The decision of the United States Court of Appeals for the Fifth Circuit is in direct conflict with recent decisions of the United States Courts of Appeals for the Seventh Circuit and the District of Columbia Circuit. In this case, the Fifth Circuit held that "we liberally[4] construes [sic] Rule 50(b) of the Federal Rules of Civil Procedure." App. 9a. The Court opined that "Peat Marwick's objections to the jury charge satisfy Rule 50(a)(2)" and concluded that "We therefore reject SHT's argument that the 1991 amendments to Rule 50(a)(2) mandate a finding of waiver." *Id.* at 10a n.14.

In distinct contrast, the United States Court of Appeals for the Seventh Circuit in recent decisions has held that the 1991 Amendment to Rule 50(a) and the Notes to the Advisory Committee have altered any prior exceptions in the case law. In *Downes v. Volkswagen of America, Inc.*, 41 F.3d 1132, 1139-1140 (7th Cir. 1994), the Seventh Circuit explained:

> Federal Rule of Civil Procedure 50 requires that a directed verdict motion must be made at the close of all evidence. In the past, this and other courts have not applied this rule rigidly, especially where a directed verdict motion was made at the close of the plaintiff's case and no prejudice has resulted to the nonmoving party from the failure to renew. *See, e.g., McKinnon v. City of Berwyn,*

4. This liberal construction of Rule 50 is in accordance with other post-1991 Fifth Circuit decisions (although it does not appear that the Fifth Circuit considered the effect of Rule 50(a), as amended, in any of these decisions). *See McArthur v. University of Tex. Health Center Tyler*, 45 F.3d 890, 896-897 (5th Cir. 1995).

> 750 F.2d 1383, 1389-90 (7th Cir.1984) (citing cases), *questioned on other grounds, Skelton v. General Motors Corp.*, 860 F.2d 250, 257 (7th Cir.1988); *see also* 9 Charles A. Wright & Arthur R. Miller, Federal Practice and Procedure § 2537 (1971). However, Rule 50 was reevaluated and amended in 1991. At that time the Advisory Committee made clear that Rule 50 deliberately "retain[ed] the requirement that a motion for judgment be made prior to the close of the trial, subject to renewal after a jury verdict has been rendered." Fed.R.Civ.P.50, Notes of Advisory Committee on Rules, 1991 Amendment. The Committee had the opportunity to change the requirements of Rule 50 in the 1991 amendments, and declined to do so. Therefore, we follow the plain language of the Rule and affirm the district court's conclusion that [defendant] was precluded from seeking j.n.o.v. because it failed to renew its directed verdict motion at the close of all the evidence.

Accord Umplehy v. Potter & Bromfield, 69 F.3d 209, 212 (7th Cir. 1995) (the Court acknowledged that *Downes* altered prior law and requires a motion for judgment at the close of the evidence); *see also Warlick v. Cross*, 969 F.2d 303, 308 n.1 (7th Cir. 1992) (although the 1991 Amendment was not yet applicable to this case, the Court noted that "the 1991 Amendments to Rule 50 may eliminate this exception") and *Moore's Federal Practice 1996 Rules Pamphlet* at ¶ 50.4 at 516 (1996) (under Rule 50(a)(2), as amended in 1991, "a motion for judgment as a matter of law must be made at the close of all the evidence if it is to be renewed after the verdict," citing *Downes*).

Similarly in *U.S. E.E.O.C. v. AIC Security Investigations, LTD*, 55 F.3d 1276 (7th Cir. 1995) the Seventh Circuit followed the plain language of Rule 50(a)(2). The Court stated that "The 1991 Amendments to Rule 50 erased the *Benson* end-around the Rule." *Id.* at 1286. The "*Benson* end-around the Rule" was the exception noted in *Benson v. Allphin*, 786 F.2d 268, 274-75 (7th Cir.), *cert. denied*, 479 U.S. 848 (1986) where the Seventh Circuit allowed a motion for directed verdict prior to the close of the evidence to preserve an issue for appellate review. This case was a case that was expressly cited by the Advisory Committee as an example of a prior exception that was altered by the 1991 Amendment. In *AIC Security*, the Seventh Circuit explained:

> Rule 50 now specifies that only a proper Rule 50(a) motion preserves the issue for later review, and that a proper motion is one that is explicitly a motion for judgment as a matter of law. "Such a motion shall specify the judgment sought and the law and the facts on which the moving party is entitled to the judgment." Rule 50(a)(2). The Advisory Committee notes to the 1991 amendment of Rule 50(a)(2) state, "The revision thus alters the result in cases in which courts have used various techniques to avoid the requirement that a motion for a directed verdict be made as a predicate to a motion for judgment notwithstanding the verdict. *E.g., Benson v. Allphin* . . . ."

786 F.2d at 1286-1287; *accord Jackson v. City of Cookeville*, 31 F.3d 1354, 1357 (6th Cir. 1994) ("the text of the rule now states that a motion for a judgment as a matter of law must be made before submission of the evidence to the jury").

Similarly, the District of Columbia Circuit has recently endorsed the plain language of Rule 50(a)(2). In *Whelan v. Abell*,

48 F.3d 1247, 1251 (D.C. Cir. 1995), the District of Columbia Circuit agreed that defendants waived an affirmative defense because they failed to raise that defense in their motion for directed verdict. The Court quoted the new language of Rule 50(a)(2), cited to the Advisory Committee Notes and commented that in the Advisory Committee Notes the "new language explicitly requiring specificity in Rule 50 motion works to 'alter[] the result' in cases where a court, by allowing less specificity effectively circumvented the requirement that the later motion be based on grounds raised in the earlier motion."[5]

As such, there is an express conflict between the Seventh Circuit and the District of Columbia Circuit on the one hand, and the Fifth Circuit and all other Court of Appeals that liberally construe Rule 50 on the other hand. *Trujillo v. Goodman,* 825 F.2d 1453, 1456 (10th Cir. 1987) (the Tenth Circuit noted the "general practice of construing liberally[6] what constitutes a motion"); *Farley Transp. Co. v. Santa Fe Transp. Co.*, 786 F.2d 1342, 1347 (9th Cir. 1985); *Mosley v. Cia. Adra. S.A.*, 362 F.2d 118, 121 (2d Cir. 1966), *cert. denied*, 383 U.S. 933 (1966).

In addition to this express conflict, there also appears to be a conflict, or at least considerable confusion, in the Circuits as to the scope of an exception to the requirements of Rule 50(a). There are some Circuits that have endorsed a broad exception to the Rule and others that have endorsed a narrow exception. *See Pulla v. Amoco Oil Co.*, 72 F.3d 648, 655 (8th Cir. 1995) (comparing the broad exception adopted by some Circuits to the

---

5. The Court concluded, however, that the plaintiff, in turn, failed to object to this procedural defect by defendants and thereby waived the issue on appeal. 48 F.3d at 1251-1252. This conclusion though does not alter the court's endorsement of the plain language of Rule 50(a)(2).

6. In *Moran v. Raymond,* 484 F.2d 1008 (7th Cir. 1973), *cert. denied,* 415 U.S. 932 (1974), the Seventh Circuit noted that the courts take a liberal view of Rule 50, however that case has been obviously overruled by the more recent Seventh Circuit cases.

narrow exception adopted by others). Under the broad exception to Rule 50, courts excuse a litigant's failure to make a motion for judgment at the close of the evidence where (1) the party files a Rule 50 motion at the close of plaintiff's case; (2) the district court defers ruling on the motion; (3) no evidence related to the claim is presented after the motion; and (4) very little time passes between the original assertion and the close of defendant's case. *See, e.g., Purcell v. Sequin State Bank & Trust Co.*, 999 F.2d 950, 956 (5th Cir. 1993); *Boynton v. TRW, Inc.*, 858 F.2d 1178, 1186 (6th Cir. 1988) (en banc); *American Protein Corp. v. AB Volvo*, 844 F.2d 56, 61 (2nd Cir. 1988), *cert. denied*, 488 U.S. 852 (1988).

By contrast, some Circuits have adopted a narrow exception to Rule 50(a). *See, e.g., DeMarines v. KLM Royal Dutch Airlines*, 580 F.2d 1193, 1195 n.4 (3d Cir. 1978) (motion for directed verdict which was handed to the judge's law clerk, but never came to the judge's attention, could not serve as the predicate to a motion for judgment n.o.v.); *Lifshitz v. Walter Drake & Sons*, 806 F.2d 1426 (9th Cir. 1986) (motion in limine and subsequent discussion with and ruling by the District Court judge were not substitute for a motion for directed verdict); *Faveline. Inv., S.A. v. Municipality of Ponce*, 645 F.2d 92, 94-95 (1st Cir. 1981) (case must be "exceptional" to overlook failure to comply with Rule 50(b)). This conflict should be rectified by this Court.

Also, there is divergence in the Circuits and to whether or not objections to jury instructions can serve as a substitute to a motion for judgment at the close of the evidence. Some Circuits, including the Fifth Circuit, have allowed objections to jury instructions to serve as a substitute for a motion. *See, e.g., Purcell*, 999 F.2d at 956; *Albrecht v. Herald Co.*, 425 F.2d 124, 127 (8th Cir. 1970), *cert. denied*, 400 U.S. 866 (1971). Other Circuits have not allowed objections to jury instructions to serve as a substitute for a motion. *See, e.g., Lewis v. Kendrick*, 944 F.2d

949, 953 (1st Cir. 1991); *Lowenstein v. Pepsi-Cola Bottling Co. of Pennsauken*, 536 F.2d 9, 12 (3rd Cir.), *cert. denied*, 429 U.S. 966 (1976); *Mallick*, 644 F.2d at 235 (3rd Cir.). This divergence, which is very unsettling to a litigant like SHT who relied upon the express language of Rule 50(a)(2) and then lost a $8,500,000 jury verdict, should be corrected by this Court.

III. The Fifth Circuit's Application Of Law Is In Violation Of *Erie* And In Conflict With Opinions Of The Fifth And Other Circuits.

In reaching its decision that Defendant Peat was not liable to SHT for negligent misrepresentation, the Fifth Circuit made an "*Erie* guess" as to how the Texas state courts would resolve this issue. In so doing, the Fifth Circuit relied on *In re: Crazy Eddie Securities Litigation*, 812 F. Supp. 338 (E.D.N.Y. 1993), a United States District Court case applying Texas law. In violation of *Erie*, the Fifth Circuit relied on *Crazy Eddie* in the face of a well-established line of cases from the intermediate Texas appellate courts which govern the issue of limited class in the context of a claim for negligent misrepresentation. *See Shatterproof Glass Corp. v. James*, 466 S.W.2d 873, 879 (Tex.Civ.App.-Ft. Worth 1971, writ ref'd. n.r.e.); *Cook Consultants, Inc. v. Larson*, 700 S.W.2d 231, 234-35 (Tex.Civ.App.- Dallas 1985, writ ref'd. n.r.e.); *Blue Bell, Inc. v. Peat, Marwick, Mitchell & Co.*, 715 S.W.2d 408, 411 (Tex.Civ.App.-Dallas 1986, writ ref'd. n.r.e.); *Hermann Hosp. v. National Standards Ins. Co.*, 776 S.W. 2d 249 (Tex.Civ.App.-Houston 1989, writ denied). *In each of these cases*, the Texas Supreme Court refused or denied the writ of error.

In 1940, this Court announced four decisions which held that a federal court must follow the precedent of an intermediate appellate court of the forum state in the absence of other persuasive data indicating how the highest court of the state would decide the issue in question. *See Stoner v. New York Life*

Ins. Co., 311 U.S.464 (1940); *West v. American Tel. & Tel. Co.*, 311 U.S. 223 (1940); *Six Cos. of California v. Joint Highway Dist. No. 13*, 311 U.S.180 (1940); *Fidelity Union Trust v. Field*, 311 U.S. 169 (1940). The principles set forth in these 1940 cases have been refined over the years to require something other than blind adherence to the decisions of intermediate appellate courts, *if other persuasive data convince the federal court that the state's highest court would decide differently;* in the absence of such data, the federal courts should and do follow the intermediate appellate decisions. *See, e.g., Eastern Mountain Platform Tennis, Inc. v. Sherwin Williams Co.*, 40 F.3d 492, 499 (1st Cir. 1994)(while not controlling, lower state court decisions are often the best indicator of how the highest court will resolve an issue); *United States v. Spaddiccino*, 800 F.2d 292, 296 (2d Cir. 1986) (deference to intermediate court's interpretation of statute); *Borse v. Piece Goods Shop, Inc.*, 963 F.2d 611, 614 (3d Cir. 1992)(intermediate state court may be "presumptive" evidence of state law); *Cross v. Cummins Engine Co.*, 993 F.2d 112, 116 (5th Cir. 1995); *Puckett v. Tennessee Eastman Co.*, 889 F.2d 1481, 1485 (6th Cir. 1989)(federal court may not disregard a decision of the state intermediate appellate court, even if a federal court has previously held to the contrary); *see generally* C. Wright, A. Miller & E. Cooper, *Federal Practice and Procedure* §4507 (1996) (and cases cited therein).

Petitioner also submits that, under *Erie*, part of the federal court's analysis of state law must take into consideration the highest court's *treatment* of the intermediate appellate decisions.

A. Texas State Law

As set forth above, four Texas cases govern SHT's claim for negligent misrepresentation. In 1971, the Texas Court of Appeals, in *Shatterproof Glass Corp. v. James*, 466 S.W.2d 873, 879 (Tex.Civ.App.-Ft. Worth 1971, writ ref'd. n.r.e.), held "that the Restatement (Second), Torts, § 552 . . . should be adopted in

Texas for application to cases [alleging negligent misrepresentation]." *Id.* at 879. Within the scope of § 552:

> [A]n accountant may be held liable to third parties who rely upon financial statements . . . prepared by the accountant in cases where the latter fails to exercise ordinary care in the preparation of such statements . . . and the third party because of such reliance suffers loss or damage.

Id. at 880. The Restatement does not require an accountant to know the identity of the recipient of the financial statements; it is only necessary that the accountant knows that the statements would be relied upon by a "group or class of persons." Restatement (Second) of Torts, § 552, comment h. It is also sufficient if the accountant knows that the recipient intends to supply the statements to a group or class of persons. *Id.*

In the mid- to late-1980's, the Texas intermediate courts revisited and expanded the concept of liability for negligent misrepresentation pursuant to the Restatement. *Cook Consultants, Inc. v. Larson,* 700 S.W.2d 231, 234-35 (Tex.Civ.App.-Dallas 1985, writ ref'd. n.r.e.), identifies four factors in determining whether the duty described in § 552 is owed in a particular case: (1) the extent to which the transaction was intended to effect the plaintiff; (2) foreseeability of harm; (3) the connection between the defendant's conduct and the injury suffered; and (4) potential liability. The *Cook* court applied § 552 to extend liability of a surveyor to "the person or class of persons whom the maker of the representation intended to benefit *or who foreseeably may be expected to rely on the information.*" *Id.* (emphasis supplied).

Blue Bell, Inc. v. Peat, Marwick, Mitchell & Co., 715 S.W. 2d 408, 411 (Tex.Civ.App.-Dallas 1986, writ ref'd. n.r.e.),

picked up where *Cook Consultants* left off. In *Blue Bell,* Peat argued that it owed no legal duty to Blue Bell because there was no privity of contract. The court disagreed, and cited to *Shatterproof Glass* to reject Peat's argument. Noting its recent opinion in *Cook Consultants,* which extended liability to persons who foreseeably may be expected to rely on the information, 715 S.W.2d at 412 n.3, the *Blue Bell* court explained that it would not limit liability to the class of third parties who may recover to those *actually known* by the defendant as indicated by Comment h, Illustration 10 under § 552:

> Consequently, we adopt a less restrictive interpretation of section 552 than would be indicated by the comments thereunder, particularly Comment h., illustration 10. To allow liability to turn on the fortuitous occurrence that the accountant's client specifically mentions a person or class of persons who are to receive the reports, when the accountant may have that same knowledge as a matter of business practice, is too tenuous a distinction for us to adopt as a rule of law. Instead, we hold that if, under current business practices and the circumstances of the case, an accountant preparing audited financial statements knows *or should know* that such statements will be relied upon by a limited class of persons, the accountant may be liable for injuries to members of that class relying on his certification of the audited reports. *See Note, Accountant's Liability,* 60 Tex. Law Rev. at 776 n. 90.

Id. at 412 (emphasis in original). The *Blue Bell* court did however, state that it found the "reasoning of the cases and

commentators urging adoption of the foreseeability test *persuasive. . . .*" *Id.* (emphasis supplied).

Hermann Hosp. v. National Standards Ins. Co., 776 S.W.2d 249 (Tex.Civ.App.-Houston 1989, writ denied)[7], applied the "should have known" standard adopted in *Blue Bell.* In *Hermann Hospital,* a case involving verification of insurance coverage, the Texas Court of Appeals reversed and remanded the grant of summary judgment in favor of the defendant, stating that "appellees *should have known* that appellant would rely on its representations of coverage in deciding whether to accept [the patient] for treatment." *Id.* at 254 (emphasis supplied). The court stated that under *Cook Consultants* and *Blue Bell,* "liability is extended to the persons whom the maker of the representation intends to benefit or who foreseeably may be expected to act in reliance on it." *Id.*

Thus, the Texas courts have adopted § 552 with a significant caveat: that liability is not limited to a class of persons who are known. This interpretation has been confirmed by the United States District Court for the Northern District of Texas. In *Steiner v. Southmark Corp.*, 734 F. Supp. 269, 272, 279-280 (N.D. Tex. 1990)("*Steiner I*"), plaintiffs purchased securities in the Southmark Corporation which had been publicly issued. Plaintiffs brought an action for negligent misrepresentation against Southmark's former accountant, alleging various

---

7. In each of the four Texas cases, the Texas Supreme Court refused or denied the writ of error. As such, that court had the opportunity on four occasions to correct any perceived error concerning limited class by the Court of Appeals, but declined to do so. Indeed, in the Application for Writ of Error submitted by Peat in the *Blue Bell* appeal, Peat made many of the same arguments to the Supreme Court concerning liability for negligent misrepresentation that it now makes before this Court. R13:Exhibit A. In response, the Texas Supreme Court ruled "that the applications present no error requiring reversal of the judgment of the Court of Appeals." R13:Exhibit B.

misrepresentations in Southmark's audited financial statements. After plaintiffs purchased their stock, Southmark announced a write-off in its assets in excess of one billion dollars. The Court stated that the "premise of each complaint is that the alleged misstatements artificially inflated the value of Southmark securities and thereby injured those who purchased the securities on the open market." *Id.* at 274. The Court held that Texas courts follow Section 552 of the Restatement and confirmed the "should have known standard":

> . . . Texas courts have held that an accountant preparing audited financial statements may be liable for misstatements that the accountant knows or *should have known* that such statements would be relied upon by a limited class of persons.

Id. at 280 (*citing Blue Bell* and *Shatterproof Glass*) (emphasis supplied). Denying the accountant's motion to dismiss, the Court noted that the scope of liability under § 552 was extended even further in *Hermann:*

> [L]iability "is extended to the persons or class of persons whom the maker of the representation intends to benefit or who foreseeably may be expected to act in reliance on it."

Id. The group of plaintiffs to which the accountant "is potentially liable is not the public at large...but instead the limited class of purchasers of Southmark securities." *Id.* Thus, under *Steiner I,* a purchaser of public securities may have a claim for negligent misrepresentation against an accountant who audits financial statements upon which the purchaser relies in making an investment decision.

Steiner v. Southmark Corp., 739 F. Supp. 1087, 1088-89

(N.D. Tex. 1990) ("*Steiner II*"), clarified the prior opinion, noting that Texas courts follow § 552 and opined that "whether a person or group of persons falls within the 'limited class' as used in § 552 is a fact issue." *Id.* (*citing Blue Bell*). The Court emphasized that *Blue Bell* rejected "strict interpretation of § 552 that would circumscribe the class to those persons actually and specifically known by" the accountant and stated "the universe of persons is instead directly related to the particular risk to which the victims were subjected." *Id.* The Court referred to the four factors identified in *Cook Consultants* and explained that liability "is at least in part a question of fact." *Id.* (*citing Cook Consultants*). Thus, the District Court confirmed the legal standard for limited class set forth above and emphasized that the scope of an accountant's duty is a question of fact.

B. The Fifth Circuit *Erie* Guess

Instead of relying on the foregoing cases, the Fifth Circuit resolved its "*Erie* guess" by relying instead on *In re: Crazy Eddie Securities Litigation*, 812 F. Supp. at 357, 360, and by selective citation to dicta in the Texas cases, the result of which was to read each case in isolation and to ignore the clear pattern of the cases when they are read together. Indeed, the Fifth Circuit wholly ignored the most recent holding in *Hermann Hospital* (1986). In *Crazy Eddie*, the New York federal court made its own "*Erie* guess" and concluded that the Texas Supreme Court would not find that an accountant owed a duty to investors seeking to acquire control through open market purchases. *Id.* at 360. Although the facts of *Crazy Eddie* are distinguishable from the instant case, the Fifth Circuit relied on *Crazy Eddie*, rather than the Texas intermediate appellate decisions. In *Crazy Eddie*, plaintiff EMI alleged that Peat negligently issued audited financial statements upon which EMI relied to purchase stock in the over-the-counter market. *Id.* Unlike the instant case, there were no allegations of any communications or contact between EMI and Peat. *Id.* Further, there were no allegations or evidence

that Peat knew of EMI's stock purchases or knew that its audit reports would be relied upon by investors. In considering Peat's motion for summary judgment, the court ignored EMI's unsupported contention that Peat knew that EMI intended to acquire control of Crazy Eddie. *Id.* at 357. The Court determined that:

> [T]hese cases do not suggest that Texas courts have or would find that accountants would owe a duty of care to a "limited class" of future major investors seeking to acquire control, *through open-market purchases of a publicly-traded company.* The *Cook* and *Blue Bell* courts both carefully cabined an accountant's duty within a "limited class" of ascertainable third persons. In both cases the plaintiffs received the very documents prepared by defendants.

Id. at 360 (emphasis supplied).

There are two reasons why *Crazy Eddie,* so heavily relied upon by the Fifth Circuit, is inapposite. First, the stock purchase in *Crazy Eddie* was simply a public transaction, with no knowledge by Peat of the stock purchases, plaintiff EMI, or reliance by investors on the audit reports. Here, the stock purchase initially was a private transaction with knowledge by Peat, there were subsequent communications by and between Peat and SHT, and there was knowledge by Peat of reliance by investors upon the audit reports. Moreover, the limited class in this case is not "unidentified future open market buyers of publicly-traded securities", but rather an ascertainable[8] group of purchasers of a controlling share of Rangaire in a private transaction known to Peat.

Second, the interpretation of Texas law in *Crazy Eddie* is misguided. As explained above, a purchaser of corporate securities, even if the securities are purchased in a public market, may have a claim for negligent misrepresentation against an accountant if the accountant knew or should have known that the purchaser would rely on the audit reports in making the investment decision.

In addition, the Fifth Circuit engaged in a rather selective reading of the Texas cases, and wholly ignored *Hermann Hospital.* App. at 17a-18a. For example, in its discussion of *Cook Consultants,* the Fifth Circuit quotes dicta, in which the *Cook* court cites to a 1974 Utah case which found that future purchasers of shares of stock could not hold an accountant liable, because the class would be unlimited. App. at 17a (*quoting Cook Consultants,* 700 S.W.2d at 236). Other than that isolated citation, the Fifth Circuit ignores the overall holding of *Cook,* which extended liability to the class of persons who "foreseeably may be expected to rely on the information." *Cook,* 700 S.W. 2d at 234-35. The panel reduced its analysis of *Blue Bell* to the following conclusory comment:

> With regard to the "limited group" requirement, the court in *Blue Bell* held that when the auditors [Peat] supplied the corporation with a number of audit reports, indicating knowledge by the auditors that third parties would be given these reports, "one of a limited number of *existing* trade creditors" was in a "limited group" so as to make summary judgment in favor of the accountants inappropriate. [Footnote

8. Peat, if it chose to, could have easily ascertained the members of such a group prior to any sale through one of four sources: (1)Roberts; (2)the Trustee in Roberts' bankruptcy, (3)Hill and (4) the investment banker.

> omitted]. This holding, however, falls far short of deciding that a *potential* investor with no previous connection to either the corporation or the accountant is within such group.

App. at 18a. Again, the Panel took an isolated fact ["existing trade creditor"] from *Blue Bell* to bolster its finding of no liability, yet ignored the holding of *Blue Bell* that whether the plaintiff falls within a "limited class" is a question of *fact.* 715 S.W.2d at 412. The *Blue Bell* court then went on to say that the fact that Blue Bell was an existing trade creditor was a relevant factor; it did not say that it was dispositive, or defined the boundaries of limited class.

The broad holding of *Hermann Hospital*, which is discussed above, was completely ignored by the Panel.

The result of what the Fifth Circuit did here was to reject the Texas state court decisions, as well as their interpretations in *Steiner I* and *Steiner II*, all of which find that "whether a person or group falls within the limited class as used in §552 [of the restatement]," is a question of fact. Instead, the Fifth Circuit found that *as a matter of law* pursuant to *Crazy Eddie*, potential investors are "generally not within a 'limited group'." App. at 18a.

Moreover, the Fifth Circuit panel in this case is in conflict with another panel, in *Comer v. Texaco Inc.*, 514 F.2d 1243(5th Cir. 1975). In that case, the Fifth Circuit found that it was significant that the state's highest court refused to review the intermediate appellate court decision in question, thus requiring the Fifth Circuit to give the intermediate appellate decision considerable weight. Here, in each of the four Texas cases, the Texas Supreme Court refused (three cases) or denied (one case) the writ of error. *See, e.g., Ohler v. Trinity Portland Cement Co.,*

181 S.W. 2d 120 (Tex. Civ. App.-Galveston1944) (decision of the Court of Civil Appeals, to which Supreme Court refuses writ of error, is as binding as decision of Supreme Court). Indeed, in the application for writ of error submitted by Peat in the *Blue Bell* appeal, Peat made many of the same arguments to the Texas Supreme Court concerning negligent misrepresentation that it made before the Fifth Circuit. R13:Exhibit A. Nevertheless, the SHT panel ignored that fact, and the refusal of the writ of error, in reaching its "*Erie* guess."

CONCLUSION

For the foregoing reasons, Petitioners the Scottish Heritable Trust, PLC and SHT Holdings (US), Inc. respectfully request that their Petition for a Writ of Certiorari be granted.

Respectfully submitted,

DALE A. COOTER
Counsel of Record
JAMES E. TOMPERT
COOTER, MANGOLD,
TOMPERT & CHAPMAN, P.L.L.C
Attorneys for Petitioners
815 Connecticut Avenue, N.W.
Suite 301
Washington, D.C. 20006
(202) 289-5600

Dated: July 29, 1996

APPENDIX A — OPINION OF THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT DATED APRIL 30, 1996

The SCOTTISH HERITABLE TRUST, PLC and SHT Holdings (US), Inc., Plaintiffs-Appellees Cross-Appellants,

v.

PEAT MARWICK MAIN & CO., a partnership and KPMG Peat Marwick, a partnership, Defendants-Appellants Cross-Appellees.

No. 94-10952.

United States Court of Appeals,
Fifth Circuit.

April 30, 1996.

* * *

Appeals from the United States District Court for the Northern District of Texas.

Before REYNALDO G. GARZA, WIENER and STEWART, Circuit Judges.

WIENER, Circuit Judge:

Defendant-Appellant Peat Marwick Main & Co. (Peat Marwick) appeals from an adverse judgment following a jury verdict that Peat Marwick is liable to a third party for negligent misrepresentations contained in audit reports. Concluding that Texas law does not permit the plaintiffs to recover in these

particular circumstances, we reverse the district court's judgment and render a take-nothing judgment in favor of Peat Marwick.

I.

FACTS AND PROCEEDINGS

The plaintiffs in this case are The Scottish Heritable Trust, PLC (SHT/PLC) and SHT Holdings (US), Inc. (SHT(US)) (collectively, SHT). SHT/PLC is a British conglomerate based in York, England. SHT/PLC owns many diverse businesses around the world and has generated annual sales in excess of $200 million. SHT(US) is a wholly-owned subsidiary of SHT/PLC which holds companies that have been acquired in the United States.

Through a series of stock purchases made in 1988, SHT acquired a controlling interest in Rangaire Corporation. Based in Cleburne, Texas, Rangaire's principal business is lime production. The stock of Rangaire is publicly traded on the National Association of Securities Dealers Automated Quotation System (NASDAQ).

SHT's investment in Rangaire ultimately proved to be unsuccessful. SHT now seeks to hold Peat Marwick—the auditor of Rangaire's financial statements from 1962 to 1990—liable for this loss. SHT claims that the audit reports with respect to the fiscal years ended July 81, 1987 and July 31, 1988 were deficient in that Peat Marwick issued an unqualified opinion on financial statements that materially overstated the net book value[1] of

---

1. Book value is generally equal to the historical cost of an asset. Net book value is equal to book value less depreciation. Neither book value nor net book value is the same as fair market value.

Rangaire's fixed assets. SHT further claims that its *justifiable reliance* on these faulty audit reports caused the loss which it sustained on the Rangaire stock.

The background and timing of SHT's stock purchases are important to this case. In 1985, Rangaire hired an investment banker for the purpose of locating a buyer for the company. Unable to find a willing buyer, Rangaire instead conducted a tender offer in which its Employee Stock Ownership Plan (ESOP) purchased stock from Rangaire's stockholders. The only evidence that Rangaire was for sale following this August 1986 tender offer consists of testimony from a former employee that some of the "major players" in the industry toured the plant facilities as prospective purchasers.[2]

Peat Marwick issued the audit reports in question on the following dates:

Report for the Fiscal Year Ended	Date Report Issued
July 31, 1987	October 7, 1987
July 31, 1988	September 30, 1988

2. The officers and directors of Rangaire would have a fiduciary duty to consider any bona fide offer for the company. In this vein, Joseph Hill, Rangaire's former President and Chief Operating Officer, testified that Rangaire would be for sale "if the right price came along."

Appendix A

SHT acquired its controlling interest in Rangaire in the following series of transactions:

Date	Percentage of Rangaire Purchased	Total Percentage Owned
August 8, 1988	28%	28%
September 30 & October 11, 1988	5%	33%
December 14 & 15, 1988	17%	50%

SHT's initial purchase of Rangaire stock was from the bankruptcy estate of Rangaire's founder and Chairman, Eugene Roberts. Roberts had filed for bankruptcy in December 1987, several months *after* Peat Marwick issued the 1987 audit report. SHT had learned of the availability of the Roberts' stock in June 1988, from an investment banker who it had retained for the purpose of locating a publicly-traded U.S. company in which to acquire a block of stock.

After SHT and its investment banker made their own independent evaluation of Rangaire, SHT acquired Roberts' 28 percent interest in the company from the bankruptcy trustee. That was on August 8, 1988, approximately 11 months after Peat Marwick issued the 1987 audit report. It is undisputed that Peat Marwick had no actual knowledge of this transaction before an agreement had been reached between SHT and Roberts' bankruptcy estate.

Following this initial purchase, Robin Garland, the Chief Executive Officer of SHT/PLC, was elected to the Rangaire board of directors. As a result, Garland had access to Rangaire's internal financial records and began to receive detailed financial

data. Garland was troubled to learn of certain accounting practices which had the effect of increasing the book value of the fixed assets as reflected on the financial statements. Concerned that this might be the "tip of the iceberg," Garland directed Robert Elliot—a partner with SHT/PLC's English auditors, Moores & Rowland—specifically to investigate, among other things, the fixed assets on Rangaire's books.

Elliot prepared a report dated September 20, 1988, which suggested that Rangaire's financial statements overstated the proper net book value of the fixed assets. The report recommended that SHT obtain an appraisal of the fixed assets to confirm (1) their existence and (2) their cost, and advised that any related write-offs would probably be treated as a prior period adjustment. This recommendation apparently was not heeded, as SHT took no immediate action on this matter.

In late September and October 1988—after the Elliot report had been completed—SHT acquired an additional 5 percent of Rangaire. This purchase was made from Eugene Roberts' family and was described by SHT as a "courtesy," whatever that may mean.

As the months passed, SHT became increasingly dissatisfied with the management of Rangaire. In an effort to oust Joseph Hill, Rangaire's President and Chief Operating Officer, SHT decided to purchase enough additional Rangaire stock to give SHT a controlling interest in the company. This final purchase occurred in December 1988 and brought SHT's ownership in Rangaire to approximately 50 percent. As with SHT's initial purchase, it is undisputed that Peat Marwick had no actual knowledge of any of SHT's subsequent purchases of Rangaire stock prior to their respective consummations.

Appendix A

In January 1989, shortly after SHT had acquired a controlling interest, SHT successfully ousted Hill and named Stephen McBride, the Chief Financial Officer of SHT/ PLC, to be Rangaire's President and Chief Executive Officer. During his six-month tenure as President, McBride made significant changes in the company's operations. McBride also instituted accounting policy changes. These accounting changes conformed with SHT's home office policies and had the effect of reducing the net book value of the fixed assets.

During the fiscal year ended December 31, 1989,[3] Rangaire wrote off millions of dollars of fixed assets which had been reflected on prior year financial statements. During its 1989 audit, Peat Marwick agreed that generally accepted accounting principles (GAAP) permitted Rangaire to take a $12.1 million write-off. A dispute arose, however, as to whether these write-offs were properly attributable to 1989 or if instead they were attributable to errors made in prior years. McBride contended that almost all of the write-offs were the correction of prior year accounting errors.[4] Rangaire's Audit Committee, however, disagreed and concluded that most of the write-offs were properly recorded in 1989. Consequently, Rangaire decided that it was not necessary to amend its prior year financial statements that Peat Marwick had audited. From 1989 through 1992,

---

3. After SHT acquired a controlling interest, Rangaire's new management changed the fiscal year end from July 31 to December 31, to conform with SHT's year end.

4. SHT claims that these write-offs are the result of the improper extension of the useful lives of the fixed assets, the improper capitalization of repairs, the continuation of assets on the books after they either ceased to exist or had been abandoned, and the capitalization of small assets normally expensed.

Appendix A

Rangaire republished the July 31, 1987, 1988, and 1989 financial statements four times without any changes. Indeed, Rangaire's new auditors, Aronson, Fetridge, Weigle & Stern, sent Peat Marwick a "comfort letter" in 1990, as well as in 1991 and 1992, stating that it had no information to indicate that Rangaire's previous financial statements needed to be restated.

The $12.1 million write-off was publicly disclosed in October 1989. Rangaire's stock price, however, did not significantly change during the several weeks following this disclosure. During the year 1990, though, Rangaire's stock price spiraled steadily downward, and SHT suffered a substantial loss on its investment when it eventually sold the stock.

It was only then that SHT brought suit against Peat Marwick, claiming security law violations and negligent misrepresentations. The jury determined that Peat Marwick was not liable for any security law violations. On the negligent misrepresentation claim, however, the jury found against Peat Marwick and awarded $8,500,000 in damages.

Peat Marwick then moved for judgment as a matter of law or, in the alternative, for a new trial. SHT moved to strike Peat Marwick's motion for judgment as a matter of law on grounds that Peat Marwick failed to make a motion for judgment at the close of all the evidence pursuant to Rule 50(b) of the Federal Rules of Civil Procedure and that Peat Marwick's objections to the jury charge did not cure this omission.

The district court denied both SHT's motion to strike and Peat Marwick's motion for a new trial. Concluding that there was insufficient evidence to support some of the damages awarded by the jury, the district court granted in part Peat Marwick's

motion for judgment as a matter of law, reducing the judgment to $4,725,000.

Both Peat Marwick and SHT now appeal on many issues related to the negligent misrepresentation claim. SHT does not challenge the negative jury verdict with respect to the security law claim.

II.

ANALYSIS

A. STANDARD OF REVIEW

We review a jury's findings of fact under the "sufficiency of the evidence" standard.[5] Under that standard, "[t]he verdict must be upheld unless the facts and inferences point so strongly and so overwhelmingly in favor of one party that reasonable men could not arrive at any verdict to the contrary. If there is evidence of such quality and weight that reasonable and fair minded men in the exercise of impartial judgment might reach different conclusions, the jury function may not be invaded."[6] A district court's application of state law is reviewed de novo.[7]

---

5. *Granberry v. O'Barr*, 866 F.2d 112, 113 (5th Cir.1988).

6. *Id.* (quoting *Western Co. of N. Am. v. United States*, 699 P.2d 264, 276 (5th Cir.), *cert. denied*, 464 U S. 892, 104 S.Ct. 237, 78 L.Ed.2d 228 (1983)).

7. *Salve Regina College v. Russell*, 499 U.S. 225, 231, 111 S.Ct. 1217, 1221, 113 L.Ed.2d 190 (1991).

Appendix A

B. WAIVER

As an initial matter, SHT argues that Peat Marwick has waived its right to challenge the sufficiency of the evidence on appeal because it failed to move for judgment as a matter of law at the conclusion of all the evidence.[8] We disagree.

Although we acknowledge that a failure to move for judgment as a matter of law at the conclusion of all the evidence may result in a waiver of the right to challenge the sufficiency of the evidence,[9] we liberally construes Rule 50(b) of the Federal Rules of Civil Procedure.[10] Technical noncompliance with Rule 50(b) may be excused in situations in which the purposes of the rule are satisfied.[11] As we have often recited, the two basic purposes of this rule are "to enable the trial court to re-examine the question of evidentiary insufficiency as a matter of law if the jury returns a verdict contrary to the movant, and to alert the opposing party to the insufficiency before the case is submitted to the jury."[12] A defendant's objection to proposed jury

---

8. FED.R.CIV.P. 50(b); *McCann v. Texas City Refining, Inc.*, 984 F.2d 667, 671 (5th Cir. 1993).

9. When no timely motion has been made, we review only whether there was *any* evidence to support the jury's verdict, regardless of its sufficiency. *Wellborn v. Sears, Roebuck & Co.*, 970 F.2d 1420, 1424 (5th Cir.1992).

10. *See Polanco v. City of Austin*, 78 F.3d 968 (5th Cir.1996) (discussing this circuit's liberal construction of Rule 50(b)).

11. *MacArthur v. University of Texas Health Ctr.*, 45 F.3d 890, 896-97 (5th Cir.1995).

12. *Id.* at 897.

instructions on grounds pertaining to the sufficiency of evidence issues it seeks to appeal may satisfy these purposes.[13]

After reviewing the record in minute detail, particularly Peat Marwick's motion for judgment as a matter of law made prior to the conclusion of all evidence and Peat Marwick's objections to the proposed jury charge, we are convinced that the purposes of Rule 50(b) have been served and that the district court properly denied SHT's motion to strike. Peat Marwick's objections to the jury charge adequately addressed the sufficiency of the evidence issues which it now seeks to appeal.[14] Under these particular circumstances, a holding that these issues have not been preserved on appeal would constitute a "slavish adherence" to the Rules, a position which we have repeatedly counseled against.[15] Accordingly, we conclude that Peat Marwick has not waived its right to challenge the sufficiency of the evidence on appeal.

---

13. *Purcell v. Seguin State Bank and Trust Co.*, 999 F.2d 950, 956 (5th Cir.1993); *Jones v. Benefit Trust Life Ins. Co.*, 800 F.2d 1397, 1401 (5th Cir.1986).

14. Our review also convinces us that Peat Marwick's objections to the jury charge satisfy Rule 50(a)(2). We therefore reject SHTs argument that the 1991 amendments to Rule 50(a)(2) mandate a finding of waiver.

15. *See, e.g., Bohrer v. Hanes Corp.*, 715 F.2d 213, 217 (5th Cir.1983), *cert. denied*, 465 U.S. 1026, 104 S.Ct. 1284, 79 L.Ed.2d 687 (1984) (stating that "[t]o demand a slavish adherence to the procedural sequence and to require these defendants, in this case, to articulate the words of renewal once the motion had been taken under advisement, would be 'to succumb to a nominalism and a rigid trial scenario as equally at variance as ambush with the spirit of the rules.' ").

Appendix A

C. ACCOUNTANTS' LIABILITY TO THIRD PARTIES FOR NEGLIGENT MISREPRESENTATION

1. *Basic Approaches*

Three basic approaches have been developed by the courts for determining the scope of accountants' liability to third parties who use and rely on their audit reports. The first approach requires either strict privity of contract or "near privity" with an auditor before he may be held liable for negligent misrepresentation.[16] "Near privity" somewhat relaxes the requirement of actual privity of contract and requires only that (1) the accountants have actual knowledge that their reports will be used for a particular purpose; (2) the accountants have actual knowledge that a nonclient is expected to rely on the reports in furtherance of a particular purpose; and (3) there has been some conduct on the part of the accountants linking them to that party, which evinces the accountants' understanding of that party's reliance.[17] This is the most restrictive view of accountants' liability to third parties and is followed by a minority of the states.

The second approach is the "foreseeability" approach. Under this one, accountants are subject to liability to third parties much like any other tortfeasor. Thus, accountants may be held liable to any third party for negligent misrepresentation if it is reasonably foreseeable that such third party might obtain and

---

16. *E.g., Ward v. Ernst & Young*, 246 Va. 317, 435 S.E.2d 628, 631 (1993) (requiring privity); *Credit Alliance Corp. v. Arthur Andersen & Co.*, 65 N.Y.2d 536, 493 N.Y.S.2d 435, 443-44, 483 N.E.2d 110, 118 (1985) (requiring "near privity").

17. *Credit Alliance Corp.*, 493 N.Y.S.2d at 443-44, 483 N.E.2d at 118.

rely on the audit report.[18] This expansive view of accountants' liability has been adopted in only a few states,[19] and some of them have recently retreated from this approach.[20]

The third approach is the one adopted by the Restatement (Second) of Torts, which provides in the relevant part:

> § 552. Information Negligently Supplied for the Guidance of Others
>
> (1) One who, in the course of his business, profession or employment, or in any other transaction in which he has a pecuniary interest, supplies false information for the guidance of others in their business transactions, is subject to liability for pecuniary loss caused to them by their justifiable reliance upon the information, if he fails to exercise reasonable care or competence in obtaining or communicating the information.

---

18. *E.g., Touche Ross & Co. v. Commercial Union Ins. Co.*, 514 So.2d 315 (Miss.1987).

19. *See First Nat'l Bank v. Monco Agency, Inc.*, 911 F.2d 1053, 1058-59 (5th Cir.1990).

20. *See Bily v. Arthur Young & Co.*, 3 Cal.4th 370, 11 Cal.Rptr.2d 51, 63, 74-75, 834 P.2d 745, 757, 769 (1992) (rejecting the foreseeability approach which had been adopted by lower courts and noting that the foreseeability approach has not attracted a substantial following and has encountered substantial criticism from commentators); *Petrillo v. Bachenburg*, 139 N.J. 472, 655 A.2d 1354, 1360 (1995) (noting that New Jersey has statutorily changed its foreseeability rule for accountants to a more restrictive test).

> (2) Except as stated in Subsection (3), the liability stated in Subsection (1) is limited to loss suffered
>
> (a) by the person or one of a limited group of persons for whose benefit and guidance he intends to supply the information or knows that the recipient intends to supply it; and
>
> (b) through reliance upon it in a transaction that he intends the information to influence or knows that the recipient so intends or in a substantially similar transaction.[21]

Although not as restrictive as the privity or "near privity" approach, the Restatement approach does not allow recovery for every reasonably foreseeable consumer of financial information.[22] Rather, the Restatement approach steers a middle course by allowing only a prescribed group of third parties to recover for pecuniary losses attributable to inaccurate financial statements. This is the approach that the majority of states have adopted. The popularity of the Restatement approach appears to be a result of many courts' finding it to be most consistent with the policy foundations underlying the tort of negligent misrepresentation.[23]

---

21. RESTATEMENT (SECOND) OF TORTS § 552 (1977).

22. *First Nat'l Bank v. Monco Agency, Inc.*, 911 P.2d 1053, 1060 (5th Cir 1990) (discussing application of the Restatement under Louisiana law).

23. *E.g., Bily v. Arthur Young & Co.*, 3 Cal.4th 370, 11 Cal.Rptr.2d 51, (Cont'd)

2. *Texas Approach*

Texas law governs this diversity case. Along with the majority of other jurisdictions, the Texas courts have adopted the Restatement approach with respect to accountants' liability to third parties for negligent misrepresentation.[24] Among the many issues raised in this appeal, Peat Marwick argues that the district court improperly applied Texas law when it concluded that SHT—a potential investor with respect to its initial purchase and an existing shareholder with respect to its subsequent purchases—could be a member of a "limited group" contemplated by the Restatement.

a. *Member of "Limited Group"*

1. *Initial Purchase*

As noted, Restatement (Second) of Torts § 552 requires that a plaintiff claiming negligent misrepresentation be the person, or a member of a "limited group" of persons, for whose benefit and guidance the defendant either intends to supply the information or knows that the recipient intends to supply it. The Restatement thus restricts the persons to whom accountants owe a duty and

---

(Cont'd)

74-75, 834 P.2d 745, 769 (1992) ("The rule expressed [in the Restatement] attempts to define a narrow class and circumscribed class of persons to whom or for whom representations are made. In this way, it recognizes commercial realities by avoiding both unlimited and uncertain liability for economic losses in cases of professional mistake and exoneration of the auditor in situations where it clearly intented to undertake the responsibility of influencing particular business transactions involving third persons.").

24. *Federal Land Bank Ass'n. v. Sloane*, 825 S.W.2d 439, 442 Tex.1991); *Blue Bell, Inc. v. Peat, Marwick, Mitchell & Co.*, 715 S.W.2d 408, 411 (Tex.App.—Dallas 1986, writ ref'd n.r.e.).

does not allow recovery for every foreseeable user of financial statements.[25] In its order addressing Peat Marwick's motion for judgment as a matter of law, the district court concluded that the "limited group" in this case was "potential purchasers of a controlling share of Rangaire."[26] Peat Marwick insists that this ruling is an improper application of Texas law.

SHT made its initial purchase of Rangaire stock in August 1988 from Eugene Roberts' bankruptcy estate in a privately negotiated transaction with the bankruptcy trustee. Peat Marwick had no actual knowledge of this transaction prior to its consummation, and SHT had no previous connection to Rangaire. At the time Peat Marwick issued the 1987 audit report, Roberts had not yet filed for bankruptcy. As SHT simply belonged to the universe of all potential investors in Rangaire, argues Peat Marwick, SHT was not a member of a "limited group" contemplated by the Restatement as a matter of law.

In support of its argument, Peat Marwick contends that Texas would follow a number of other jurisdictions that have held potential investors not to be members of a "limited group."[27]

---

25. *See First Nat'l Bank v. Monco Agency, Inc.*, 911 F.2d 1053, 1060 (5th Cir. 1990).

26. We are troubled by the fact that this legal determination was not announced until after the jury had entered a verdict. The jury asked for assistance on this issue while it was deliberating, but received no guidance as to the boundaries of a limited group. Even if the court's post-verdict statement were legally correct, and even if SHT fit that definition when it made its initial purchase—which is highly problematic—there is nothing to indicate that the jury had any guidance as to the limits of the group.

27. *E.g., In re ML-Lee Acquisition Fund II, L.P.*, 848 F.Supp. 527, 556

(Cont'd)

As one court has explained, to interpret the "limited group" requirement as including all potential investors would render that requirement meaningless.[28]

Peat Marwick argues further that the district court's ruling that the "limited group" in the instant case consisted of potential purchasers of a controlling interest of Rangaire rather than all potential investors, does not save it from error. In support of this contention, Peat Marwick relies on *In re Crazy Eddie Securities Litigation*,[29] an analogous case in which Texas law also governed.

In re Crazy Eddie involved a situation in which the auditors knew at the time they issued the audited financial statements that its client was "in play" as a potential takeover target.[30] After analyzing the same Texas authorities relied on by SHT in the instant case, the district court concluded that "these cases do not suggest that Texas courts have or would find that accountants owe a duty of care to a 'limited class' of future major investors seeking to acquire control, through open-market purchases, of a publicly-traded company."[31] The court further stated that:

(Cont'd)
(D.Del.1994); *In re Crazy Eddie Sec. Litig.*, 812 F.Supp. 338, 360 (E.D.N.Y.1993); *In re Sahlen & Assoc. Sec. Litig.*, 773 F.Supp. 342, 374 (S.D.Fla.1991).

28. *In re ML-Lee Acquisition Fund II, L.P.*, 848 F.Supp. 527, 556 (D.Del.1994) (quoting *Brug v. Enstar Group, Inc.*, 755 F.Supp. 1[illegible]7, 1258 (D.Del.1991)).

29. 812 F.Supp. 338 (E.D.N.Y.1993).

30. *In re Crazy Eddie*, 812 F.Supp. at 357.

31. *Id.* at 360.

> Plaintiffs have not cited, and the court cannot find, a single decision by any court extending an accountant's duty of care to as-yet unidentified future open-market buyers of publicly-traded securities, even when that duty is limited to the rarified class of buyers with sufficient resources to acquire control of entire companies.
>
> This court believes that the Texas Supreme Court is unlikely to adopt a rule so universally avoided by sister states.[32]

The Texas courts have not had occasion to decide this particular aspect of the "limited group" requirement, so we must make an *Erie* guess as to how the Texas courts would come down on this issue. Although the authorities discussed above have no binding effect on this court, we conclude that their analysis accurately represents Texas law. To hold that a potential purchaser, even one of a controlling interest, is generally not a member of a "limited group" contemplated by the Restatement is consistent with the Restatement's objective of restricting accountants' liability to a prescribed group and not allowing recovery for all foreseeable users of an accountants' audit report. Moreover, the Texas courts have intimated this same view, albeit in dicta. In *Cook Consultants*, a negligent misrepresentation case in which the defendant was a surveyor, the Texas court stated that "[u]nlike, for example, future purchasers of shares of stock attempting to hold an accountant liable, [plaintiff] Larson is not a member of an unlimited class. . . ."[33]

---

32. *Id.* (internal citations omitted).

33. *Cook Consultants v. Larson*, 700 S.W.2d 231, 236 (Tex.App.—Dallas 1985, writ ref'd n.r.e.).

Relying on cases such as *Blue Bell*,[34] SHT insists that Texas law is more expansive than the Restatement approach and permits a finding that Peat Marwick owed SHT a duty in this context. We disagree.

In *Blue Bell*, the court held that actual knowledge of a particular plaintiff or class of plaintiffs is not necessary if the defendant should have had this knowledge.[35] To this extent, Texas law is indeed less restrictive than the Restatement. *Blue Bell*, however, in no way abandoned the "limited group" requirement. Indeed, the court expressly declined an invitation to adopt the foreseeability approach.[36]

With regard to the "limited group" requirement, the court in *Blue Bell* held that when the auditors supplied the corporation with a number of audit reports, indicating knowledge by the auditors that third parties would be given these reports, "one of a limited number of *existing* trade creditors" was in a "limited group" so as to make summary judgment in favor of the accountants inappropriate.[37] This holding, however, falls far short of deciding that a potential investor with no previous connection to either the corporation or the accountant is within such group. As stated above, we conclude that such a potential investor is generally not within a "limited group" under Texas law.

---

34. *Blue Bell, Inc. v. Peat, Marwick, Mitchell & Co.*, 715 S.W.2d 408, 411 (Tex.App.—Dallas 1986, writ ref'd n.r.e).

35. *Id.* at 412.

36. *Id.*

37. *Id.* at 413 (emphasis added).

SHT further insist that the question whether an accountant owes a duty to a third party is in part a fact question.[38] SHT thus makes much of the testimony of Peat Marwick partners that they knew that investors in general might rely on audited financial statements. SHT also notes that Eugene Roberts had cash flow problems many years before his filing for bankruptcy and that it is a reasonable inference to assume that he would sell his stock in the company.[39] These and similar facts and inferences, argues SHT, are enough to permit a conclusion that SHT was a member of a "limited group." We again disagree.

We acknowledge SHT's contention that the question whether an accountant owes a duty to a third party is in part a fact question.[40] The outer boundaries of a "limited group" referred to in the Restatement, however, is a legal determination. Although we do not suggest that a potential purchaser can never be a member of a "limited group," the facts in this particular case, even when viewed in a light most favorable to the jury's verdict, simply do not provide a nexus sufficient to bring a potential investor like SHT within the ambit of the "limited group" requirement. To predicate an accountants' duty to third parties on such things as the general knowledge that accountants possess about typical investors or tenuous inferences concerning future events would be to eviscerate the Restatement rule in favor of a de facto foreseeability approach—an approach which the Texas courts have refused to embrace.

---

38. *See Steiner v. Southmark Corp.*, 739 F.Supp. 1087, 1088 (N.D.Tex1990) (Texas law).

39. We note that Roberts received approximately $5 million dollars from the August 1986 tender offer prior to his filing for bankruptcy.

40. *See Steiner*, 739 F.Supp. at 1088.

We therefore conclude that as a matter of law Peat Marwick owed SHT no duty with respect to SHT's initial purchase of Rangaire stock.

2. *Subsequent Purchases*

With respect to the several stock purchases following its initial purchase, SHT occupied the status of an existing minority-interest shareholder. Peat Marwick argues that an existing shareholder, like a potential investor, also is not a member of a "limited group." Indeed, at least one jurisdiction has accepted this argument.[41] Nevertheless, as the other issues raised on appeal by Peat Marwick even more clearly mandate a reversal in this case, we simply assume without deciding that SHT could be a member of a "limited group" with respect to its subsequent stock purchases.

b. *Justifiable Reliance*

In addition to the "limited group" requirement discussed above, the Restatement requires that a plaintiff justifiably rely on the information that the defendant negligently misrepresents.[42] Like the Restatement, Texas law requires that a plaintiff claiming negligent misrepresentation prove that its reliance was justifiable.[43]

---

41. *Machata v. Seidman & Seidman*, 644 So.2d 114, 116 (Fla.App.1994), *review denied*, 654 So.2d 919 (Fla.1995).

42. RESTATEMENT (SECOND) OF TORTS § 552(1) (1977).

43. *Airborne Freight Corp. v. C.R. Lee Enter., Inc.*, 847 S.W.2d 289, 294 (Tex.App.—El Paso 1992, writ denied).

Appendix A

As the words of the phrase imply, *justifiable reliance* comprises two elements: (1) the plaintiff must in fact rely on the information; and (2) the reliance must be reasonable.[44] The justifiableness of the reliance is judged in light of the plaintiff's intelligence and experience.[45] For purposes of the tort of negligent misrepresentation, reliance is unjustified when the relying party is negligent.[46]

Peat Marwick argues that as a matter of law SHT cannot prove justifiable reliance. As we have concluded that SHT was not a member of a "limited group" with respect to its first purchase of Rangaire stock, we only address justifiable reliance with respect the subsequent purchases.

SHT has vast and sophisticated experience in acquiring both public and private businesses around the world. In addition, SHT placed its Chief Executive Officer on Rangaire's board of directors and had access to virtually all of Rangaire's internal financial records. Well in advance of SHT's second stock purchase, Garland, SHT's CEO, learned of and was concerned by questionable accounting practices which had the effect of inflating the book value of Rangaire's fixed assets. Garland's concerns were later confirmed by Elliot, SHT's long-time advisor. Elliot recommended an appraisal of the fixed assets to

---

44. *Geosearch, Inc. v. Howell Petroleum Corp.*, 819 F.2d 521, 526 (5th Cir. 1987).

45. *See Haralson v. E.F. Hutton Group, Inc.*, 919 F.2d 1014, 1026 (5th Cir. 1990).

46. *Id.* at 1025, n. 5; see RESTATEMENT (SECOND) OF TORTS § 552A (1977) (barring recovery for negligent misrepresentation if the recipient of the misrepresentation is negligent in so relying).

determine their existence and cost, and advised SHT on how to treat the related writ-offs. Yet SHT now claims to have justifiably relied on Peat Marwick's negligent misrepresentations involving an overstatement of the net book value of Rangaire's fixed assets.

Given that prior to making the subsequent stock purchases, SHT (1) was an extremely sophisticated multi-national conglomerate; (2) had virtually complete access to the internal financial records of Rangaire; and (3) suspected, and was later warned by its advisor, that a problem existed regarding the book value of fixed assets which it now complains that Peat Marwick failed to detect or disclose, we find it simply incredible that SHT could have been justified in relying on the audit reports in question, if in fact it relied on them at all.[47] And even when we view the evidence in the light most favorable to the verdict, we must conclude that no reasonable jury could arrive at a verdict to the contrary.[48] We therefore hold as a matter of law that if SHT did indeed rely on Peat Marwick's audit report with respect to its stock purchases following the initial acquisition, such reliance was simply unjustified.

---

47. *See id.* at 1026 (citing *Grumman Allied Indus., Inc. v. Rohr Indus., Inc.*, 748 F.2d 729, 737 (2d Cir. 1984) and suggesting that Texas courts, like New York courts, are "particularly disinclined to entertain claims of justifiable reliance when sophisticated plaintiff has access to information that would reveal fraud at a time when harm could be averted.").

48. We cannot help but speculate that the failure to submit separate jury questions with respect to the different stock purchases may in large part explain the jury's finding.

D. OTHER ISSUES

As we conclude that SHT either was not within a "limited group" or lacked justifiable reliance as to all of its purchases of Rangaire stock, we need not and therefore do not address Peat Marwick's other arguments. We note in passing, however, that some of the other issues raised by Peat Marwick, such as loss causation and damages, have considerable merit. Similarly, we do not address SHT's arguments regarding the district court's reduction of damages, as our take-nothing judgment makes that issue moot.

III.

CONCLUSION

With respect to its first purchase of Rangaire stock, SHT was not a member of a "limited group," as contemplated by the Restatement and Texas law. With respect to all subsequent purchases, SHT lacked justifiable reliance as a matter of law. Therefore under Texas law SHT is not entitled to recover against Peat Marwick for negligent misrepresentation. Accordingly, the judgment of the district court is reversed and a take nothing judgment in favor of Peat Marwick is rendered.

REVERSED and RENDERED.

APPENDIX B — ORDER OF THE UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF TEXAS, DALLAS DIVISION FILED SEPTEMBER 26, 1994

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION

CIVIL ACTION NO.
3:90-CV-1634-P

THE SCOTTISH HERITABLE TRUST, PLC, and SHT HOLDINGS (US), INC.,

v.

PEAT MARWICK MAIN & CO. and KPMG PEAT MARWICK

ORDER

Before the court are:

1) Defendant's Motion for Judgment Notwithstanding the Verdict and, in the Alternative, Motion for New Trial, filed December 30, 1993, and brief in support;

2) Plaintiffs' Opposition to Motion for Judgment Notwithstanding the Verdict and, in the Alternative, Motion for New Trial, filed February 28, 1994;

3) Defendant's Reply Brief in Support of Defendant's Motion for Judgment Notwithstanding the Verdict and, in the Alternative, Motion for New Trial, filed March 28, 1994;

4) Plaintiffs, Motion to Strike Defendants' Motion For

Judgment Notwithstanding the Verdict, filed January, 26, 1994; and

5) Defendant's Opposition to Plaintiffs' Motion to Strike Defendant's Motion for Judgment Notwithstanding the Verdict, filed February 16, 1994.

Plaintiffs are The Scottish Heritable Trust, PLC, and SHT Holdings (US), Inc., and the Defendant is Peat Marwick Main & Co. In 1988, Plaintiffs purchased a controlling share of stock in Rangeaire, a company located in Cleburne, Texas. Defendant Peat Marwick was Rangeaire's accountant and was responsible for preparing audit reports after conducting audits on Rangeaire's records. Plaintiffs allege that some time after their purchase of Rangeaire, they discovered that the audit reports prepared by Peat Marwick for the years 1987 and 1988 were faulty in that the reports overstated the value of some of Rangeaire's assets and listed as assets items that were no longer in existence, not in use, or were of no value. In 1989, Plaintiffs wrote off several million dollars of Rangeaire's assets. Plaintiffs alleged that this had an adverse affect on the value of Rangeaire causing Plaintiffs to lose money. Plaintiffs brought claims for federal securities laws violations and for negligent misrepresentations. The case was tried before a jury, and on December 9, 1993, the jury returned a verdict in favor of Plaintiffs on the negligent misrepresentation claim, and awarded Plaintiffs $8,500,000.00 in damages.

Defendant seeks to set aside the jury verdict on the basis that at the time it issued its 1987 audit report, it had no knowledge of Plaintiffs' contemplated purchase of Rangeaire. Defendant also argues that it had no knowledge that Plaintiffs would purchase additional shares of Rangeaire stock when it issued its 1988 audit

report. Because of these facts, Defendant argues that Plaintiffs were not members of the limited group for whose benefit the audit reports were intended.

The court submitted to the jury, Question No. 10, which asked: "Do you find from a preponderance of the evidence that Plaintiffs belong to the limited group of persons for whose benefit and guidance the Defendants intended to supply the information or for whom Defendants knew or should have known the recipients intended to supply the information?" The jury answered "yes" to this question. The court is of the opinion that the question properly reflected Texas law on the issue of accountant liability to third parties. *Blue Bell Inc. v. Peat, Marwick. Mitchell & Co.*, 715 S.W. 2d 408 (Tex.App. — Dallas,1986, writ ref'd. n.r.e.); *Hermann Hospital v. National Standards Insurance Co.*, 776 S.W. 2d 249 (Text App.— Houston [1st Dist.] 1989, writ denied); *Steiner v. Southmark Corp.*, 739 F.Supp. 1087 (N.D. Tex. 1990). These cases also hold that the issue of whether a plaintiff falls within the limited group to which an accountant may be liable is, at least in part, a fact question. In this case, the court agrees with Defendant that the limited group was not potential investors in Rangeaire. The group was potential purchasers of a controlling share of Rangeaire. It is not necessary that the defendant knew the specific identity of the plaintiff, it is only necessary that they knew the identity of the group. Restatement (Second) of Torts, §552, comment h. Texas has expanded liability to include a limited group that defendants should have known about. *Blue Bell*, supra. There was evidence before the jury from which it could find that Plaintiff was a member of the group of potential buyers of Rangeaire, and that Peat Marwick knew or should have known of the existence of that group. Further, there was evidence from which the jury could find that any member of the group of

potential purchasers of Rangeaire would be supplied with the audit reports prepared by Peat Marwick. Defendant asserts that Rangeaire was not for sale in 1987 and 1988, and cites testimony from Mr. Mack Hill, President of Rangeaire, that it was not for sale after 1986. The fact remains that Rangeaire had been looking for a purchaser, had hired an investment bank in 1985 to help locate a buyer, and was sold in 1988. There was conflicting testimony as to whether Rangeaire was for sale in 1987 and 1988, and it was for the jury to decide by making credibility determinations and weighing all, and not selected portions, of the evidence. The jury decided these issues against Defendant, and the court cannot say that those jury decisions were not supported by the evidence.

Damages

The jury awarded Plaintiffs $8.5 million in damages. The jury was asked to consider three categories of damages. The court is in agreement with Defendant that the evidence does not support a portion of the damages awarded. The first category of damages was "the difference between the price Plaintiffs paid for the investment and what the investment was worth at the time of purchase." Plaintiffs' expert testified that Plaintiffs suffered $6.1 million in damages in this category, and the jury awarded $6 million. In this category of damages, Plaintiffs' expert testified to: 1) $2.1 million in damages because Rangeaire capitalized repairs; 2) $1.3 million damages because spare parts with an individual value of less than $500.00 were improperly capitalized; and 3) $1.5 million was improperly taken in depreciation because it related to the improper capitalization of repairs. There was no evidence from an accountant, accounting expert, or anyone else, that the capitalization of repairs, or carrying as assets parts with individual value of less than

$500.00, was improper under United States accounting principles. There was testimony from some of Plaintiffs' officers that such practice was improper under United Kingdom practice. However, the evidence was that such practices are proper under United States accounting practice, and involve judgment calls. The court therefore finds that the jury's award of $2.1 million for capitalized repairs and $1.3 million for carrying as assets certain parts is not supported by the evidence. Additionally, the $1.5 million for depreciation which related to the capitalized repairs is also not supported by the evidence. This is a total of $4.9 million of which Plaintiffs claimed 50%. Therefore, the court will grant Defendant's Motion for Judgment Notwithstanding the Verdict as to $2.45 million of the jury's damage award under the first category and reduce the damages in that category to $3.55 million.

The third category of damages that the jury was asked to consider was "additional out of pocket expenses." Here Plaintiffs were seeking $1.5 million due to refinancing the Rangeaire loans from Ameritrust, refinancing of the parent company's debt in 1991, and for excess audit fees charged by Peat Marwick. There was no testimony that the refinancing fees were related to or resulted from the writeoffs taken by Plaintiffs in 1989 as a result of the over statement of assets in the audit reports. Therefore, the court grants Defendant's Motion for Judgment Notwithstanding the Verdict as to the refinancing costs, but not as to the excess audit fees. Therefore, the amount of damages in the third category is reduced from $1.5 million to $175,000. The total damages award will be $4,725,000.00.

The Defendant's Motion for Judgment Notwithstanding the Verdict is Denied in all other respects. Defendant's Motion for New Trial is Denied.

Appendix B

Plaintiffs' Motion to Strike Defendant's Motion for Judgment Notwithstanding the Verdict is Denied.

The court will enter an Amended Final Judgment in accordance with this Order.

SO ORDERED.

SIGNED this 26th day of September, 1994.

s/ Jorge A. Solis
JORGE A. SOLIS
UNITED STATES DISTRICT JUDGE

APPENDIX C — SECOND AMENDED FINAL JUDGMENT OF THE UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF TEXAS, DALLAS DIVISION FILED SEPTEMBER 26, 1994

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION

3:90-CV-1634-P

THE SCOTTISH HERITABLE TRUST PLC, and SHT HOLDINGS (US), INC.,

Plaintiffs,

v.

PEAT MARWICK MAIN & CO. and KPMG PEAT MARWICK

Defendants.

SECOND AMENDED FINAL JUDGMENT

This civil action was tried to a jury, which returned its verdict on December 9, 1993. Having considered the applicable law and the jury's findings, the Court hereby **ORDERS and ADJUDGES** as follows:

Pursuant to the jury's verdict of December 9, 1993, and the Court's order of September 26, 1994, it is **ORDERED** that Plaintiffs the Scottish Heritable Trust, PLC, and SHT Holdings (US), Inc., have judgment against Defendants Peat Marwick Main & Co. and KPMG Peat Marwick in the amount of $4,725,000.00.

Appendix C

Also, Plaintiffs are hereby awarded post-judgment interest from December 16, 1993 at the rate of 3.61% per annum.

IT IS FURTHER ORDERED that the above-entitled and numbered cause be, and it is hereby, **CLOSED** with all court costs taxed against Defendants.

SIGNED this 26th day of September, 1994.

s/ Jorge A. Solis
JORGE A. SOLIS
UNITED STATES DISTRICT JUDGE

APPENDIX D — RELEVANT STATUTES

The 1991 Amendment to Rule 50(a) of the Federal Rules of Civil Procedure is shown as follows (matter stricken out is in brackets; new matter is in italics):

> Rule 50. [Motion for a Directed Verdict and for] Judgment [Notwithstanding the Verdict] as a Matter of Law in Actions Tried by Jury; Alternative Motion for New Trial; Conditional Rulings.
>
> (a) [Motion for a Directed Verdict; When Made; Effect. A party who moves for a directed verdict at the close of the evidence offered by an opponent may offer evidence in the event that the motion is not granted, without having reserved the right so to do and to the same extent as if the motion had not been made. A motion for a directed verdict which is not granted is not a waiver of trial by jury even though all parties to the action have moved for directed verdicts. A motion for a directed verdict shall state the specific grounds therefor. The order of the court granting a motion for a directed verdict is effective without any assent of the jury.]
>
> *Judgment as a Matter of Law*
>
> *(1) If during a trial by jury a party ha been fully heard with respect to an issue and there is no legally sufficient evidentiary basis for a reasonable jury to have found for that party with respect to that issue, the court may*

grant a motion for judgment as a matter of law against that party on any claim, counterclaim, cross-claim or third party claim that cannot under the controlling law be maintained without a favorable finding on that issue.

(2) Motions for judgment as a matter of law may be made at any time before submission of the case to the jury. Such a motion shall specify the judgment sought and the law and the facts on which the moving party is entitled to the judgment.

Supreme Court, U.S.
FILED
AUG 29 1996
CLERK

No. 96-153

In The

Supreme Court of the United States

October Term, 1995

THE SCOTTISH HERITABLE TRUST, PLC and SHT HOLDINGS (US), INC.,

Petitioners,

v.

PEAT MARWICK MAIN & CO. and KPMG PEAT MARWICK,

Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Fifth Circuit

RESPONDENTS' BRIEF IN OPPOSITION

MORRIS HARRELL*
TIMOTHY W. MOUNTZ
CYNTHIA KEELY TIMMS
LOCKE PURNELL RAIN HARRELL
(A Professional Corporation)
2200 Ross Avenue, Suite 2200
Dallas, Texas 75201-6776
214/740-8000

DAVID M. PYKE
RADER, CAMPBELL, FISHER & PYKE
2777 Stemmons Freeway
Stemmons Place, Suite 1080
Dallas, Texas 75207
214/630-4700

ANTHONY J. COSTANTINI
SUTHERLAND, ASBILL & BRENNAN
600 Madison Avenue, 11th Floor
New York, New York 10022
212/605-6410

Attorneys for Respondents

*Counsel of Record

COCKLE LAW BRIEF PRINTING CO., (800) 225-6964
OR CALL COLLECT (402) 342-2831

QUESTIONS PRESENTED

1. Whether the 1991 amendments to Rule 50 preclude a ruling that a defendant complied with the requirement of moving for judgment as a matter of law at the close of all the evidence when defendant (1) objected to the sufficiency of the evidence on specific grounds both in its jury charge objections and in an unrecorded charge conference; (2) asked that the issues not be submitted to the jury; (3) had objected to the sufficiency of the evidence on specific grounds before and during the trial; and (4) during its jury charge objections, renewed its prior motion for judgment as a matter of law and its summary judgment motion.

2. Whether a court of appeals' *Erie* analysis on an issue of state law not previously addressed by either the state's highest or intermediate courts was proper where the court of appeals had before it all relevant authorities, and these authorities provide support for the court's conclusion.

LIST OF PARTIES TO PROCEEDING PURSUANT TO RULES 14.1(b) AND 29.6

Pursuant to Supreme Court Rule 14.1(b), Respondents certify that the names of all parties to this proceeding appear in the caption of the Brief of Respondents, except that Respondents' name has changed since the time of trial to KPMG Peat Marwick LLP.

Pursuant to Supreme Court Rule 29.6, Respondents are not corporations and have no parent companies or nonwholly owned subsidiaries.

TABLE OF CONTENTS

Page

STATEMENT OF JURISDICTION 1

STATEMENT OF THE CASE 1

A. Course of Proceedings Below 2

B. Background Regarding Negligent Misrepresentation Cause of Action 2

C. Background Regarding Rule 50 Arguments .. 6

REASONS WHY THE PETITION SHOULD BE DENIED 8

I. THERE IS NO TRUE CONFLICT BETWEEN THE CIRCUITS AND THE GRANTING OF A WRIT WOULD BE PREMATURE 8

A. SHT's Question on the Rule 50 Issue is Too Broad 8

B. The Rule 50 Question is Narrow and There is No Conflict on That Narrow Issue 9

C. There is No Conflict Even With Regard to the Broad Question SHT Poses 12

D. It Would be Premature for This Court to Consider the Rule 50 Issue 14

E. Conclusion 15

II. THE FIFTH CIRCUIT'S DECISION ON THE RULE 50 ISSUE IS FACT AND CASE SPECIFIC AND IS THE CORRECT DECISION 15

A. The Decision on the Rule 50 Issue is Fact and Case Specific 15

B. The Fifth Circuit's Decision Is Correct 17

1. The Purposes of Rule 50 Were Fulfilled .. 17

TABLE OF CONTENTS – Continued

Page

2. The 1991 Amendments to Rule 50 Do Not Support SHT's Arguments 18

3. There is Ample Support for the Fifth Circuit's Decision on the Rule 50 Question 20

4. Conclusion 22

III. THERE IS NO CONFLICT THAT WOULD PERMIT THE GRANTING OF A WRIT ON THE ISSUE OF THE FIFTH CIRCUIT'S *ERIE* ANALYSIS 22

IV. THE FIFTH CIRCUIT WAS THOROUGHLY JUSTIFIED IN MAKING ITS *ERIE* ANALYSIS IN THIS CASE 23

A. The Fifth Circuit's Approach Was Entirely Consistent With a Proper *Erie* Analysis 23

B. The Fifth Circuit's Conclusion on the Issue of Texas State Law Is Well Supported 25

CONCLUSION 30

TABLE OF AUTHORITIES

Page

CASES

Acosta v. Honda Motor Co. Ltd., 717 F.2d 828 (3rd Cir. 1983) 10

Albrecht v. Herald Co., 452 F.2d 124 (8th Cir. 1971)... 10, 20

American Protein Corp. v. AB Volvo, 844 F.2d 56 (2d Cir.), *cert. denied*, 488 U.S. 852 (1988)..... 9

Anderson v. United Telephone Co., 933 F.2d 1500 (10th Cir.), *cert. denied*, 502 U.S. 940 (1991)..... 10

Bachtel v. Mammoth Bulk Carriers, 605 F.2d 438 (9th Cir. 1979), *judgment vacated on other grounds*, 451 U.S. 978 (1981) 10

Bayamon Thom McCann, Inc. v. Miranda, 409 F.2d 968 (1st Cir. 1969) 9

Beaumont v. Morgan, 427 F.2d 667 (1st Cir.), *cert. denied*, 400 U.S. 882 (1970) 9

Benson v. Allphin, 786 F.2d 268 (7th Cir.), *cert. denied*, 479 U.S. 848 (1986) 12, 19

Bernhardt v. Polygraphic Company of America, Inc., 350 U.S. 198 (1956) 23

Bonjorno v. Kaiser Aluminum & Chem. Corp., 752 F.2d 802 (3rd Cir. 1984), *cert. denied*, 477 U.S. 908 (1986) 10, 20, 21

Boynton v. TRW, Inc., 858 F.2d 1178 (6th Cir. 1988) 10

Chemical Leaman Tank Lines, Inc. v. Aetna Casualty & Surety Co., No. 93-5777, ___ F.3d ___, 1996 WL 344922 (3rd Cir. June 20, 1996)..... 11

Comer v. Texaco Inc., 514 F.2d 1243 (5th Cir. 1975) 28

TABLE OF AUTHORITIES – Continued

Page

Cook Consultants v. Larson, 700 S.W.2d 231 (Tex. App. – Dallas 1985, writ ref'd n.r.e.) 26, 28

In re Crazy Eddie Securities Litigation, 812 F. Supp. 338 (E.D.N.Y. 1993) 27

Downes v. Volkswagen of America, Inc., 41 F.3d 1132 (7th Cir. 1994) 12

EEOC v. AIC Security Investigations, Ltd., 55 F.3d 1276 (7th Cir. 1995) 11

Erie R.R. Co. v. Tompkins, 304 U.S. 64 (1938) 22

Farley Transp. Co. v. Santa Fe Trail Transp. Co., 786 F.2d 1342 (9th Cir. 1986) 21

Federal Land Bank Ass'n v. Sloane, 825 S.W.2d 439 (Tex. 1991) 25

First Nat'l Bank of Commerce v. Monco Agency Inc., 911 F.2d 1053 (5th Cir. 1990) 25

Hermann Hosp. v. National Standard Ins. Co., 776 S.W.2d 249 (Tex. App. – Houston [1st Dist.] 1989, writ denied) 26, 27

Huddleston v. Dwyer, 322 U.S. 232 (1944) 24

Jones v. Benefit Trust Life Ins. Co., 800 F.2d 1397 (5th Cir. 1986) 10

Kladis v. Brezek, 823 F.2d 1014 (7th Cir. 1987) 10, 20

Lewis v. Kendrick, 944 F.2d 949 (1st. Cir. 1991) 21

Lowenstein v. Pepsi-Cola Bottling Co., 536 F.2d 9 (3rd Cir.), *cert. denied*, 429 U.S. 966 (1976) 21

Mallick v. International Broth. of Elec. Workers, 644 F.2d 228 (3d Cir. 1981) 21

TABLE OF AUTHORITIES – Continued

Page

McCray v. New York, 461 U.S. 961 (1983) 14

Miller v. Premier Corp., 608 F.2d 973 (4th Cir. 1979) 10

Moran v. Raymond Corp., 484 F.2d 1008 (7th Cir. 1973), *cert. denied*, 415 U.S. 932 (1974)..... 10

Mosley v. Cia. Mar. Adra, S.A., 362 F.2d 118 (2nd Cir.), *cert. denied*, 385 U.S. 933 (1966)..... 10

National Indus., Inc. v. Sharon Steel Corp., 781 F.2d 1545 (11th Cir. 1986)..... 20

Neely v. Martin K. Eby Construction Co., Inc., 386 U.S. 317 (1967) 22

Pittsburgh-Des Moines Steel Co. v. Brookhaven Manor Water Co., 532 F.2d 572 (7th Cir. 1976) 10

Pulla v. Amoco Oil Co., 72 F.3d 648 (8th Cir. 1995) 17

Repola v. Morbark Indus. Inc., 934 F.2d 483 (3rd Cir. 1991)..... 10

Rice v. Sioux City Cemetery, 349 U.S. 70 (1955) 12, 13, 14, 17, 23, 29

Riverview Investments, Inc. v. Ottawa Community Improvement Corp., 899 F.2d 474 (6th Cir.), *cert. denied*, 498 U.S. 855 (1990)..... 10

Rockport Pharmacy, Inc. v. Digital Simplistics, Inc., 53 F.3d 195 (8th Cir. 1995).....10, 11

Rubinstein v. Collins, 20 F.3d 160 (5th Cir. 1994) 25

Simon v. Navon, 71 F.3d 9 (1st Cir. 1995) 11, 20, 21

Singer v. Dungan, 45 F.3d 823 (4th Cir. 1995) 10, 11

TABLE OF AUTHORITIES – Continued

Page

Shatterproof Glass Corp. v. James, 466 S.W.2d 873 (Tex. Civ. App. – Fort Worth 1971, writ ref'd n.r.e.) 26

The Monrosa v. Carbon Black Export, Inc., 359 U.S. 180 (1958) 29

Trujillo v. Goodman, 825 F.2d 1453 (10th Cir. 1987) 10

Umpleby v. Potter & Bromfield, 69 F.3d 209 (7th Cir. 1995) 11, 13

Villanueva v. McInnis, 723 F.2d 414 (5th Cir. 1984) 10

Whelan v. Abell, 48 F.3d 1247 (D.C. Cir. 1995).....11, 13

STATUTES AND RULES

Fed.R.Civ. P. 1 19

Fed.R.Civ. P. 50 ..... *passim*

Supreme Court Rule 10 .....9, 13

Tex. R. App. P. 130 27

28 U.S.C. § 1254(1) 1

MISCELLANEOUS AUTHORITIES

Charles A. Wright & Arthur R. Miller, *Federal Practice & Procedure*, § 2537 (1995) 19

Charles A. Wright, Arthur R. Miller & Edward H. Cooper, *Federal Practice & Procedure*, § 4507 (1996) 24

James W. Moore, *Moore's Federal Practice*, ¶ 50.08 (1995) 17

Restatement (Second) of Torts § 552 (1977)...24, 25, 26

RESPONDENTS' BRIEF IN OPPOSITION

Respondents Peat Marwick Main & Co. and KPMG Peat Marwick respectfully request that this Court deny the petition for writ of certiorari seeking review of the Fifth Circuit's judgment in this case. The Fifth Circuit's opinion is reported at 81 F.3d 606 (5th Cir. 1996).

STATEMENT OF JURISDICTION

SHT asserts jurisdiction pursuant to 28 U.S.C. § 1254(1). As stated below, the decision of the court of appeals in this case does not create any conflicts and does not meet the criteria of Supreme Court Rule 10 for granting a writ of certiorari.

STATEMENT OF THE CASE

SHT's "Statement of the Case" is an exercise in advocacy advancing an unfounded version of the "facts." Some of the "facts" in SHT's argumentative discussion are simply wrong; in other places, the statements made to this Court are extremely misleading.

Unlike SHT's Statement of the Case, the first four pages of the Fifth Circuit's opinion contain a full and fair presentation of the relevant facts. (81 F.3d 607-10) The appellate court's factual discussion is incorporated herein by Peat Marwick in its entirety.

In this Response, Peat Marwick will correct certain of Petitioners' factual misstatements, but will not address all of them as many are immaterial to the issues before this Court.

A. Course of Proceedings Below

Petitioners Scottish Heritable Trust, PLC, a British conglomerate with a history of corporate acquisitions, and its wholly owned subsidiary SHT Holdings (U.S.), Inc. (collectively "SHT") sued the U.S. accounting partnership of Peat Marwick Main & Co. and its successor KPMG Peat Marwick (collectively "Peat Marwick") in connection with SHT's purchases of the stock of Rangaire Corporation ("Rangaire"), a publicly-traded company for which Peat Marwick was the independent auditor. SHT bought approximately 50% of Rangaire's stock in a series of purchases. SHT asserted that the initial August 1988 purchase was made in reliance upon Rangaire's July 31, 1987 audited financial statements and that it relied on Rangaire's July 31, 1988 audited financial statements in making the subsequent purchases. When Rangaire later experienced losses while under SHT's management, SHT sued Peat Marwick claiming that the net book value of Rangaire's fixed assets was overstated in the 1987 and 1988 financial statements audited by Peat Marwick. Peat Marwick prevailed on all the federal securities law claims submitted to the jury; SHT's jury verdict was based on a pendent claim of negligent misrepresentation under Texas state law.

B. Background Regarding Negligent Misrepresentation Cause of Action

In its Petition, SHT states that Rangaire retained an investment banker to sell the company in 1985, that Peat Marwick knew of the continual search for a buyer since that time, and that Rangaire remained on the market until

purchased by SHT in 1988. (Petition,[1] p. 2) To the contrary, the record shows (as the Fifth Circuit noted) that Rangaire retained an investment banker to sell the company in 1985, but those efforts were unsuccessful and the company instead conducted a tender offer in 1986 in which its Employee Stock Ownership Plan purchased stock from Rangaire's stockholders. (81 F.3d at 608) In fact, SHT's representatives testified that when they had approached Rangaire about purchasing some stock in the summer of 1988, Rangaire's CEO initially rebuffed them and stated that, in the CEO's view, Rangaire was not for sale. (R15:109) Further, there is no evidence that – had Rangaire actually been for sale after 1985 – Peat Marwick knew anything about it. The only evidence Rangaire was for sale after 1986 was testimony from one of its plant supervisors located in another state who testified that potential purchasers had toured his plant from 1985 forward, but his testimony made clear that Peat Marwick was not aware of any such visits. (81 F.3d at 608; R29:272-73) Finally, Rangaire never was "sold" as contemplated in 1985; SHT merely acquired the stock of Rangaire's principal stockholder Eugene Roberts and later bought more stock in open-market purchases.

SHT also states that "Peat Marwick knew that [Rangaire's] audited statements would be relied upon by the investing public in a purchase of the Roberts stock." (Petition, p. 3) To the contrary, Peat Marwick's 1987 audit report on Rangaire's financial statements was issued in October 1987. (81 F.3d at 608) Roberts did not file for

---

[1] SHT's Petition for Writ of Certiorari in this Court is referred to as the "Petition." The volumes of the record will be referred to as, *e.g.*, (R10:121) (Record Volume 10, p. 121).

bankruptcy until December 1987.[2] (*Id.*) There is no evidence that Peat Marwick was aware at the time of its October 1987 report that Roberts would be filing for bankruptcy. In fact, Peat Marwick's most current information on Roberts' finances was that Roberts had received $5 million from the Rangaire tender offer just a year before. (R40:23-26) It was also undisputed that SHT's negotiations to purchase Rangaire stock from Roberts were not known by Peat Marwick until after SHT agreed to buy the stock. (81 F.3d at 608) Similarly, Peat Marwick had no knowledge of SHT's subsequent purchases of Rangaire stock before the purchases occurred. (*Id.* at 609)

SHT's Petition also misleads the Court by suggesting that SHT did not learn of alleged accounting problems at Rangaire or begin its own investigation until "the Summer of 1989," at which time it had completed its stock purchases. (Petition, p. 4) This statement is contradicted by the undisputed facts:

> Well in advance of SHT's second stock purchase [in September and October 1988], Garland, SHT's CEO, learned of and was concerned by questionable accounting practices which had the effect of inflating the book value of Rangaire's fixed assets.

---

[2] Another example of SHT's misleading statements is its assertion that subsequent to Roberts' bankruptcy filing, "*Rangaire* retained an investment banker to arrange for a sale of, *at the very least*, the Roberts stock." (Petition, p. 3; emphasis added). The investment banker was hired by Roberts' bankruptcy trustee and not Rangaire, and there is no evidence whatsoever he had authority to attempt to sell anyone else's Rangaire stock. (R49:217-21)

. . .

> Concerned that this might be the "tip of the iceberg," Garland directed Robert Elliot – a partner with SHT/PLC's English auditors, Moores & Rowland – specifically to investigate, among other things, the fixed assets on Rangaire's books. (81 F.3d at 615, 608)

The Fifth Circuit went on to note that Elliot's confidential report to SHT's CEO, which was completed on September 20, 1988, contained an action recommendation to obtain appraisals of Rangaire's fixed assets but it "apparently was not heeded as SHT took no immediate action on this matter." (*Id.* at 609) Thus, SHT made its later purchases of Rangaire stock only after (1) the fixed asset issue had surfaced, (2) it had commissioned its own accountant to investigate and report on this issue, and (3) its officers had become members of Rangaire's Board of Directors with "access to Rangaire's internal financial records" and all "detailed financial data." (*Id.* at 608)[3]

---

[3] There are many other "facts" relating to the merits of SHT's claims that the record does not support or directly contradicts. These include SHT's assertions that Hill "exercised complete domination" over Rangaire's accounting systems, that Hill began to "cook the books" of Rangaire in 1985, that Rangaire was only "marginally profitable," that Rangaire was "forced" to make the 1989 accounting writeoff, and that the result of the writeoff was "catastrophic." (Petition, pp. 2, 3, 4) The inventory test count (Petition, p. 3) related to an immaterial portion of the overall inventory in a subsequent year. (R40:173-77) These allegations were central to SHT's securities fraud claim, which the jury resolved in Peat Marwick's favor. Moreover, the Fifth Circuit expressed grave doubts as to whether the writeoff caused SHT any damage whatsoever, much less the purported "catastrophic" result, when it

C. Background Regarding Rule 50 Arguments

After the completion of discovery and before trial began, Peat Marwick moved for summary judgment on all of SHT's pending claims. (R5:1102-72) This motion, which was fully briefed, was denied on the eve of trial. At the close of SHT's case, Peat Marwick moved for judgment as a matter of law on all counts. (R36:185-87, 194-96) The motion was based, as SHT acknowledged, on many of the same grounds presented in Peat Marwick's summary judgment motion. (R36:188) The trial court denied the motion for judgment. In its ruling, however, the trial court stated that it would consider further the individual counts between that time and the time the charge was prepared and leave out counts at that stage if necessary. (R36:196)

At the specific moment in time all the evidence closed, the motion for judgment was not renewed; however, Peat Marwick effectively made such a motion by challenging the sufficiency of the evidence in several ways before submission of the case to the jury. That night, the district judge conducted a lengthy unrecorded charge conference that lasted approximately 4½ hours. As a result of that conference, SHT withdrew two of its claims and the trial court "directed out" a third claim. (R52:54) Peat Marwick then made objections to the jury charge on various grounds, including the sufficiency of the evidence on the two substantive points upon which the Fifth

---

stated that Peat Marwick's loss causation arguments had "considerable merit." (81 F.3d at 615)

Circuit ultimately focused.[4] (R52:8-9) During these objections, Peat Marwick specifically renewed its prior motions for judgment as a matter of law and for summary judgment. Counsel for SHT acknowledged during the charge objections that the objections were consistent with the discussion that had taken place at the charge conference. (R52:10-11)

The jury subsequently found for Peat Marwick on the federal securities claims but found in favor of SHT on the pendent claim of negligent misrepresentation under Texas law, and awarded SHT $8,500,000. Peat Marwick renewed its motion for judgment as a matter of law in its motion for judgment notwithstanding the verdict. (R9:2157) SHT moved to strike that motion, alleging that Peat Marwick had failed to comply with Rule 50(a). (R10:2231) The trial judge denied the motion to strike, and granted in part and denied in part the JNOV motion, reducing the judgment to $4,725,000. (R10:2327) SHT did not make a subsequent Rule 50(c)(2) motion for new trial.

Both sides appealed to the Fifth Circuit. The Fifth Circuit denied SHT's cross-appeal. As to Peat Marwick's appeal, the Fifth Circuit held that, as a matter of law, (1) SHT failed to prove a negligent misrepresentation cause of action against Peat Marwick with regard to the first

---

[4] For example, in its charge objections, Peat Marwick argued that the negligent misrepresentation claim "should not be submitted to the jury" in part because "[p]laintiffs have failed to prove and are simply not in a limited class." (R52:9) Earlier, in its motion for summary judgment, Peat Marwick argued that "[p]laintiffs have failed to demonstrate that they fall within the limited group of persons entitled to recover [for negligent misrepresentation]." (R5:1149)

stock purchase because SHT was not a member of any "limited group" and (2) SHT did not justifiably rely on the audited financials for the subsequent stock purchases.[5] The Court of Appeals reversed the trial court's judgment and rendered judgment for Peat Marwick. SHT did not file a petition for rehearing or request a new trial.

Before ruling on the merits, the Fifth Circuit addressed the question of whether Peat Marwick had complied with Rule 50. In considering this question, the Fifth Circuit decided that the trial court's determination that Peat Marwick had complied with Rule 50 was correct, "after reviewing the record in minute detail." (81 F.3d at 610) The Fifth Circuit also considered Rule 50(a)(2) as amended and held Peat Marwick had complied with that rule. (*Id.* at 611 n.14)

REASONS WHY THE PETITION SHOULD BE DENIED

I. THERE IS NO TRUE CONFLICT BETWEEN THE CIRCUITS AND THE GRANTING OF A WRIT WOULD BE PREMATURE

A. SHT's Question on the Rule 50 Issue is Too Broad

The standard by which this Court determines whether to grant a petition for writ of certiorari is whether there are "compelling reasons" for granting the

[5] The Fifth Circuit also noted that several other issues raised by Peat Marwick and not made the basis of the court's decision, such as loss causation and damages, had "considerable merit." (81 F.3d at 615)

writ. Sup.Ct.R. 10. In an effort to make the question in this case appear "compelling," SHT claims that a significant conflict exists between the circuits concerning Rule 50's requirement that a motion for judgment be made at the close of all the evidence as a prerequisite to a post-verdict motion for judgment. To try to create that supposed conflict, SHT defines its first question in an inappropriately broad fashion which is not supported by this record, and then states this is an important question which affects "every civil jury trial in the United States District Courts. . . . " (Petition, p. 6) The actual Rule 50 question presented by this case is quite narrow and would affect only those rare cases involving virtually identical factual circumstances.

B. The Rule 50 Question is Narrow and There is No Conflict on That Narrow Issue

The true question in this case is whether a defendant complies with Rule 50 when, after the close of all the evidence, that party raises sufficiency of the evidence challenges in its objections to the charge and also renews its motions for directed verdict and for summary judgment but does not formally nominate these actions as a "motion for judgment." There is no conflict between the circuits on this question.[6]

---

[6] Virtually every other circuit has previously excused, in appropriate circumstances, the fact that a formal motion for judgment was not made at the precise time the evidence closed. *See, e.g., Beaumont v. Morgan*, 427 F.2d 667, 670 (1st Cir.), *cert. denied*, 400 U.S. 882 (1970); *Bayamon Thom McCann, Inc. v. Miranda*, 409 F.2d 968, 970-72 (1st Cir. 1969); *American Protein Corp. v. AB Volvo*, 844 F.2d 56, 61-62 (2d Cir.), *cert. denied*, 488

Prior to the 1991 amendments to Rule 50, at least four circuits specifically permitted sufficiency of the evidence objections made either in the charge conference or during the charge objections to serve as a Rule 50 motion for directed verdict. *Kladis v. Brezek*, 823 F.2d 1014, 1017 (7th Cir. 1987); *Jones v. Benefit Trust Life Ins. Co.*, 800 F.2d 1397, 1401 (5th Cir. 1986); *Villanueva v. McInnis*, 723 F.2d 414, 416-18 (5th Cir. 1984); *Bonjorno v. Kaiser Aluminum & Chem. Corp.*, 752 F.2d 802, 814-15 (3rd Cir. 1984), *cert. denied*, 477 U.S. 908 (1986); *Albrecht v. Herald Co.*, 452 F.2d 124, 127 (8th Cir. 1971).

Since the 1991 amendments, only the Fifth Circuit has squarely addressed the question of whether charge objections can act as a motion for judgment as a matter of law. However, the Third Circuit has explicitly reiterated its

---

U.S. 852 (1988); *Mosley v. Cia. Mar. Adra, S.A.*, 362 F.2d 118, 121-22 (2nd Cir.), *cert. denied*, 385 U.S. 933 (1966); *Repola v. Morbark Indus. Inc.*, 934 F.2d 483, 488-89 (3rd Cir. 1991); *Acosta v. Honda Motor Co. Ltd.*, 717 F.2d 828, 831-32 (3rd Cir. 1983); *Singer v. Dungan*, 45 F.3d 823, 827-28 (4th Cir. 1995); *Miller v. Premier Corp.*, 608 F.2d 973, 979 n.3 (4th Cir. 1979); *Riverview Investments, Inc. v. Ottawa Community Improvement Corp.*, 899 F.2d 474, 477-78 (6th Cir.), *cert. denied*, 498 U.S. 855 (1990); *Boynton v. TRW, Inc.*, 858 F.2d 1178, 1184-86 (6th Cir. 1988); *Kladis v. Brezek*, 823 F.2d 1014, 1017 (7th Cir. 1987); *Pittsburgh-Des Moines Steel Co. v. Brookhaven Manor Water Co.*, 532 F.2d 572, 575-77 (7th Cir. 1976); *Moran v. Raymond Corp.*, 484 F.2d 1008, 1010-14 (7th Cir. 1973), *cert. denied*, 415 U.S. 932 (1974); *Rockport Pharmacy, Inc. v. Digital Simplistics, Inc.*, 53 F.3d 195, 197-98 (8th Cir. 1995); *Albrecht v. Herald Co.*, 452 F.2d 124, 127 (8th Cir. 1971); *Bachtel v. Mammoth Bulk Carriers*, 605 F.2d 438, 441-42 (9th Cir. 1979), *judgment vacated on other grounds*, 451 U.S. 978 (1981); *Anderson v. United Telephone Co.*, 933 F.2d 1500, 1503-04 (10th Cir.), *cert. denied*, 502 U.S. 940 (1991); *Trujillo v. Goodman*, 825 F.2d 1453, 1455-56 (10th Cir. 1987).

prior rule since the amendments, which is that "[a]n objection to a jury charge can serve as a predicate for a later Rule 50(b) motion only if the district court explicitly treated the objection as a Rule 50(a) motion." *Chemical Leaman Tank Lines, Inc. v. Aetna Casualty & Surety Co.*, No. 93-5777, ___ F.3d ___, 1996 WL 344922 at *16 (3rd Cir. June 20, 1996) (deciding the test was not met under the facts of the case and further finding charge objections did not raise the issue later presented). Since the amendments, the First Circuit has also held that a discussion with the court in chambers at the end of the evidence can serve as a motion for judgment as a matter of law. *Simon v. Navon*, 71 F.3d 9, 14 (1st Cir. 1995). In recent cases involving the amended rule, other circuits have also permitted deviation from the strict application of Rule 50 that SHT urges. *See Rockport Pharmacy, Inc. v. Digital Simplistics, Inc.*, 53 F.3d 195, 197-98 (8th Cir. 1995); *Singer v. Dungan*, 45 F.3d 823, 827-28 (4th Cir. 1995).

Peat Marwick has not found any cases – either before or after the rule amendments – that reject the general principle that objections to the charge or discussions conducted during charge conferences can, at least under some circumstances, serve as a motion for judgment. The cases that SHT cites in support of its supposed conflict do not deal with this particular issue. *See* Petition, pp. 15-18; *Umpleby v. Potter & Bromfield*, 69 F.3d 209, 212 (7th Cir. 1995) (motion for judgment at close of plaintiff's case, but not renewed at close of all evidence); *EEOC v. AIC Security Investigations, Ltd.*, 55 F.3d 1276, 1286-87 (7th Cir. 1995) (no motion for judgment at close of evidence and no mention of motion any time prior to the verdict); *Whelan v. Abell*, 48 F.3d 1247, 1251 (D.C. Cir. 1995) (particular ground on which judgment sought not mentioned

prior to verdict); *Downes v. Volkswagen of America, Inc.*, 41 F.3d 1132, 1139-1140 (7th Cir. 1994) (party precluded from seeking judgment n.o.v. because of failure to renew motion for judgment at close of evidence).

When the Fifth Circuit's actual holding in this case is considered, there is no conflict between the circuits. The Fifth Circuit's holding is entirely in accord with the decisions of all of the other circuits which have considered this issue. This Court has held "it is very important" that it be consistent in not granting certiorari in conflict situations except "in cases where there is a real and embarrassing conflict of opinion and authority between the circuit courts of appeal." *Rice v. Sioux City Cemetery*, 349 U.S. 70, 79 (1955) (quoting *Layne & Bowler Corp. v. Western Well Works, Inc.*, 261 U.S. 387, 393 (1923)). That is not the case here.

C. There is No Conflict Even With Regard to the Broad Question SHT Poses

There is no conflict between the circuits even when the question posed by SHT, which is not presented by this case, is examined on the merits. SHT cites no case discussing actual conflicts between the circuits, as opposed to minor differences concerning the application of Rule 50 in a variety of factual circumstances.

Prior to the 1991 amendments, the Seventh Circuit appears to have been the most generous of the circuits in forgiving a party's failure to move for directed verdict at the close of all the evidence. *See, e.g., Benson v. Allphin*, 786 F.2d 268, 273-74 (7th Cir.), *cert. denied*, 479 U.S. 848 (1986) (stating that Rule 50 is not strictly enforced provided that the failure to renew the motion for directed

verdict did not "unduly prejudice his opponent"). Unquestionably, the Seventh Circuit has reacted to the 1991 amendments by reining in its own expansive standards with regard to Rule 50. *See, e.g., Umpleby v. Potter & Bromfield*, 69 F.3d 209, 212 (7th Cir. 1995). However, it has done so only in circumstances where it was clear that no pre-submission motion or any facsimile thereof was made at any time after the evidence closed. (*See* pp. 11-12, *infra*) The Seventh Circuit has not stated that nothing less than a formal, officially-designated motion for judgment at the precise moment all the evidence closes will suffice as a Rule 50 motion.

SHT also argues that the District of Columbia Court of Appeals is in conflict with the Fifth Circuit's opinion in this case. Petition, pp. 17-18; *Whelan v. Abell*, 48 F.3d 1247, 1251 (D.C. Cir. 1995). There is no such conflict. The D.C. Circuit has only stated that the issue raised in the post-verdict motion for judgment n.o.v. must have been made in the pre-submission motion for judgment, relying on authority from nearly ten years before the 1991 amendments. That circuit's contribution to the alleged "conflict" is merely that it cited to and quoted from the Advisory Committee Notes to the 1991 rule amendments.

Indeed, the apparent "conflict" upon which SHT relies is with the Advisory Committee Notes to the rules, and not a conflict between the courts of appeals. This Court's rules and opinions, however, emphasize the need for a conflict between the courts of appeals. Sup.Ct.R. 10; *Rice v. Sioux City Cemetery*, 349 U.S. 70, 79 (1955). Even the alleged conflict with the Advisory Committee Notes is highly questionable. The Notes cited by SHT did not address Rule 50(b), which is the only rule that mentions renewal of a motion for judgment as a matter of law

"made at the close of the evidence." The Notes only comment upon the second sentence of new Rule 50(a)(2) with its requirement that the party moving for judgment articulate the factual and legal basis for the motion. Rule 50, Advisory Committee Notes, 1991 Amendment. Because of its limited nature, the Note itself is far too amorphous to create a conflict.

D. It Would be Premature for This Court to Consider the Rule 50 Issue

Another reason there is no conflict is that the Rule 50 question, even as framed by Petitioners, involves amendments to the rules that were adopted only as recently as 1991. By the time cases were tried under those new rules, courts of appeals were not interpreting them until two or three years after the amendments were adopted. At this point, there are few circuit opinions applying the 1991 amendments in any context. Consequently, it would be premature to grant a petition for writ of certiorari at this juncture. As this Court has written, it "should not risk inconclusive and divisive disposition of a case when time may further illumine or completely outmode the issues in dispute." *Rice v. Sioux City Memorial Park Cemetery, Inc.*, 349 U.S. 70, 77 (1955); *accord, McCray v. New York*, 461 U.S. 961, 962-63 (1983) (Stevens, J.) (denying certiorari where there presently was no conflict of decision in the federal system because "further consideration of the substantive and procedural ramifications of the problem by other courts will enable us to deal with the issue more wisely at a later date").

E. Conclusion

There is no conflict between the courts of appeal on the Rule 50 issue, either as the issue is stated by SHT or on the more accurate question Peat Marwick has presented. Furthermore, it is much too soon after the 1991 amendments to Rule 50 to speculate whether any serious conflict will develop between the courts of appeal concerning those rule changes. For these reasons alone, this Court should deny the petition. There are, however, additional reasons discussed below as to why the Court should refuse to grant certiorari.

II. THE FIFTH CIRCUIT'S DECISION ON THE RULE 50 ISSUE IS FACT AND CASE SPECIFIC AND IS THE CORRECT DECISION

A. The Decision on the Rule 50 Issue is Fact and Case Specific

In this case, there was a 4½ hour charge conference with the district court, and objections to the charge were made after the close of all the evidence and before the case was submitted to the jury. This is the time during the trial when a party would be expected to make a formal motion for judgment as a matter of law. Moreover, in the course of presenting its objections to the charge, Peat Marwick specifically raised its sufficiency objections and stated that it was "renewing" its prior motion for directed verdict and its motion for summary judgment. On this basis, Peat Marwick complied with Rule 50 without the necessity of reliance on any exceptions to that rule.

The trial court treated the discussion that occurred at the charge conference as addressing the sufficiency of the evidence to submit SHT's causes of action to the jury. Over SHT's objections, it dismissed one of SHT's claims at that juncture. (R52:54) SHT obviously also treated the charge conference as addressing the sufficiency of the evidence. As a result of the discussions that took place at that conference, SHT withdrew two of its causes of action and its request for punitive damages. (R52:3) The subsequent jury charge objections clearly raised sufficiency issues.

Following the jury's verdict, Peat Marwick filed a motion for judgment notwithstanding the verdict in which it renewed its motion for judgment as a matter of law. SHT responded to that motion with a motion to strike, asserting that Peat Marwick had not filed a motion for judgment as a matter of law at the close of all the evidence. In that motion, SHT raised the same arguments that it urges in its Petition to this Court. Moreover, in pressing its motion to strike, SHT conceded that certain issues (including the two issues on which the Fifth Circuit subsequently ruled) had been raised by Peat Marwick in both the charge conference and the objections to the charge. (R10:2300) The trial judge, who participated in the charge conference and heard the objections, denied SHT's motion to strike and granted the motion for judgment n.o.v. in part. In essence, the trial judge – who had knowledge of what had transpired before the case was submitted to the jury – agreed that Peat Marwick had complied with Rule 50.

This case is very fact-intensive. Peat Marwick's challenge to the sufficiency of Petitioners' evidence was detailed and extensive. Neither the Fifth Circuit's nor the

trial court's decision turns on a generalized rule of law, but on the specifics of who said what and when. This case is one in which this Court, rather than being free to consider broader points of law, will be mired in the record and the nuances of what the trial participants said and meant. The Fifth Circuit arrived at its conclusion that Peat Marwick had complied with Rule 50 after "reviewing the record in minute detail." (81 F.3d at 610) This Court does not "sit for the benefit of the particular litigants" nor does it take cases with only "isolated significance." *See Rice v. Sioux City Memorial Park Cemetery*, 349 U.S. 70, 74, 76 (1955). Yet that is precisely what this Court will be required to do if it takes this case.

B. The Fifth Circuit's Decision Is Correct

1. The Purposes of Rule 50 Were Fulfilled

The Fifth Circuit's decision in this case was the correct one. Courts and commentators agree that Rule 50(a) has twin purposes: to "(1) enable the trial court to examine all of the evidence before submitting the question to the jury; and (2) alert the opposing party to any defect in its case, thereby affording it an opportunity to cure any such defects." *Pulla v. Amoco Oil Co.*, 72 F.3d 648, 655 n.8 (8th Cir. 1995); *see also* 5A James W. Moore, *Moore's Federal Practice*, ¶50.08, p. 50-88 (1995). There is no question in this case that the purposes of Rule 50 were met.

From the outset, Peat Marwick repeatedly lodged the same complaints concerning SHT's evidence that it raised in its post-verdict motion. For example, with respect to the limited group issue, Peat Marwick had previously raised its post-verdict arguments both in its motion for

summary judgment (R5:1102) and in its objections to the charge. (R52:8-9) Moreover, SHT agreed in its post-trial briefing that Peat Marwick had also raised the limited group issues in the charge conference. (R10:2300) The justifiable reliance issue was also raised both during the objections to the charge and, as SHT again admitted in its post-judgment briefing, during the charge conference. (R52:7; R10:2300)

The trial court obviously felt that it had adequate notice of Peat Marwick's challenges to the evidence because it denied SHT's motion to strike the motion for JNOV and, in fact, granted the JNOV motion in part. (R10:2332) And the reality is that, between the time the evidence closed and the time the jury commenced deliberations, Peat Marwick informed SHT of the very deficiencies of which Peat Marwick complained on appeal. SHT made no attempt to correct the deficiencies. When SHT attempted to argue to the trial court that it had not received adequate notice, the trial judge–who was there – rejected that argument.

2. The 1991 Amendments to Rule 50 Do Not Support SHT's Arguments

What SHT advocates is that a draconian level of strictness be read into Rule 50, when this rule has historically been construed to determine whether its purposes have been served.[7] In essence, SHT urges that a Rule 50

---

[7] The historic construction is consistent with the general admonition that the federal procedural rules are to be "construed and administered to secure the just . . .

motion for judgment must be made in a ritualistic manner at a single precise moment to preserve sufficiency of the evidence arguments. There is no indication in the 1991 changes to Rule 50 that such a result was intended.

The Advisory Committee Notes to the 1991 amendments state that the courts of appeals should not use techniques to avoid requiring motions for judgment at the close of all the evidence such as was used in *Benson v. Allphin*, 786 F.2d 268, 272-275 (7th Cir.), *cert. denied*, 479 U.S. 848 (1986). The Seventh Circuit's opinions, as demonstrated by *Benson*, reflected an excessively permissive approach to Rule 50. For example, in *Benson*, the Seventh Circuit forgave the defendant's failure to move for judgment at the close of all the evidence, even though there had been no preverdict attempt to renew a prior motion. In fact, the defendant did not even suggest that it would like to move for judgment until after the jury began deliberating; indeed, a motion was only made after the jury had determined the liability issue.

There is no indication from the express language of the Rule change that it was intended to eliminate every deviation from the making of a formal motion for judgment at the precise moment that the evidence closes. *See, e.g.*, 9A Charles A. Wright & Arthur R. Miller, *Federal Practice & Procedure*, § 2537, p. 335 (1995) (noting that the 1991 amendments to Rule 50 changed the terminology, but "[n]o change in the substance of the motion was intended by the amendment, however"). And the cases that the Seventh Circuit has decided since the rule

---

determination of every action." Fed.R.Civ.P. 1; *see also* footnote 6, *supra*.

amendments do not address the question of what that circuit would do if the parties made the equivalent of a motion for judgment by telling the court during the charge conference and the charge objections that the evidence was insufficient for the case to be submitted to the jury. *Cf. Kladis v. Brezek*, 823 F.2d 1014, 1017 (7th Cir. 1987) (raising issue at instruction conference laid foundation for later post-verdict motion).

3. There is Ample Support for the Fifth Circuit's Decision on the Rule 50 Question

What the Fifth Circuit did in this case is supported by decisions from many of the various circuits. For a great number of years, the courts of appeals have permitted objections to the submission of claims to the jury, when based on the insufficiency of the evidence, to serve as a motion for directed verdict. *See, e.g., Simon v. Navon*, 71 F.3d 9, 14 (1st Cir. 1995) (discussion in chambers after close of evidence was functional equivalent of a motion for judgment as a matter of law); *Kladis v. Brezek*, 823 F.2d 1014, 1017 (7th Cir. 1987) (discussion at charge conference); *Bonjorno v. Kaiser Aluminum & Chem. Corp.*, 752 F.2d 802, 814-15 (3rd Cir. 1984), *cert. denied*, 477 U.S. 908 (1986) (colloquy with district court concerning jury instruction suffices as motion for directed verdict if the district court treated it as such); *Albrecht v. Herald Co.*, 452 F.2d 124, 127 (8th Cir. 1971) (objections to proposed charge supported filing of motion for judgment n.o.v.); *see also National Indus., Inc. v. Sharon Steel Corp.*, 781 F.2d 1545, 1548-49 (11th Cir. 1986) (renewal of motion for directed verdict at the beginning of the charge conference met requirements

of the rule); *Farley Transp. Co. v. Santa Fe Trail Transp. Co.*, 786 F.2d 1342, 1347 (9th Cir. 1986) (statement in dicta that "an objection to a jury instruction on the ground that insufficient evidence was presented on an issue to allow it to be submitted to the jury" may be a sufficient approximation of a motion for directed verdict).[8]

The Advisory Committee Notes to the 1991 rule changes also support the Fifth Circuit's holding in this case. After the discussion of the *Benson* case, the Notes specifically state: "The information required with the motion may be supplied by explicit reference to materials and argument previously supplied to the court." Rule 50, Advisory Committee Notes, 1991 Amendment. During its charge objections before the case was submitted to the jury, Peat Marwick specifically referred to and renewed its motion for summary judgment and its prior motion for directed verdict.

---

[8] SHT cites to three cases from two different circuits that supposedly have refused to allow objections to jury instructions to serve as a substitute for a motion for directed verdict. Petition, pp. 19-20; *Lewis v. Kendrick*, 944 F.2d 949, 953 (1st Cir. 1991) (court requested motion in writing which was never filed); *Lowenstein v. Pepsi-Cola Bottling Co.*, 536 F.2d 9, 11-12 (3rd Cir.), *cert. denied*, 429 U.S. 966 (1976); *Mallick v. International Broth. of Elec. Workers*, 644 F.2d 228, 234 (3d Cir. 1981). The situation in each of those cases was that, under the particular circumstances of the case, the court held the objections would not substitute for the motion. None of those opinions held that charge objections *would never* suffice as a motion for directed verdict. Indeed, both of the cited circuits have held that either objections to the charge or conferences on the jury submissions can serve as a motion for directed verdict. *Simon v. Navon*, 71 F.3d 9, 14 (1st Cir. 1995); *Bonjorno v. Kaiser Aluminum & Chem. Corp.*, 752 F.2d 802, 814-15 (3d Cir. 1984), *cert. denied*, 477 U.S. 908 (1986).

4. Conclusion

There is ample support for the Fifth Circuit's conclusion that the purposes of Rule 50 were served in this case. Moreover, there is no legitimate conflict among the courts of appeals on this issue.[9] As a result, this Court should deny the petition for writ of certiorari.

III. THERE IS NO CONFLICT THAT WOULD PERMIT THE GRANTING OF A WRIT ON THE ISSUE OF THE FIFTH CIRCUIT'S *ERIE* ANALYSIS

Just as with the Rule 50 question, there is no conflict between the courts of appeals on SHT's question relating to the application of *Erie R.R. Co. v. Tompkins*, 304 U.S. 64 (1938). Certainly, the Fifth Circuit did not pronounce any propositions of law that conflict with any statements of this Court or any other court of appeals. SHT asserts merely that the Fifth Circuit ignored a "well-established line of cases from the intermediate Texas appellate courts which govern the issue of limited class. . . . " (Petition, p. 20) SHT cited these Texas cases to the Fifth Circuit and the court found that they did not directly address the issue in this case. At bottom, the Fifth Circuit followed the correct *Erie* process and SHT is simply seeking another review of Texas law by this Court.

---

[9] This case presents no Seventh Amendment issue. (Petition, pp. 13-14) To the extent that SHT is complaining about being deprived of a right to a jury trial, it waived that right when it failed to request a new trial either in the district court or in the court of appeals. *Neely v. Martin K. Eby Construction Co., Inc.*, 386 U.S. 317, 330 (1967).

Moreover, if this Court took this case, it is unclear what general issues of the law it would be addressing, other than to reiterate the same well-established criteria for making *Erie* determinations the Court has already addressed. *E.g., Bernhardt v. Polygraphic Company of America, Inc.*, 350 U.S. 198, 202-04 (1956). SHT's specific *Erie* question has significance only for the parties to this case. Since this Court does not "sit for the benefit of the particular litigants" or take cases with only "isolated significance," the *Erie* issue in this case is particularly inappropriate for this Court's attention. *Rice v. Sioux City Memorial Park Cemetery*, 349 U.S. 70, 74, 76 (1955).

IV. THE FIFTH CIRCUIT WAS THOROUGHLY JUSTIFIED IN MAKING ITS *ERIE* ANALYSIS IN THIS CASE

A. The Fifth Circuit's Approach Was Entirely Consistent With a Proper *Erie* Analysis

Petitioners' argument with respect to a purported divergence from *Erie* reveals a fundamental misunderstanding of the types of issues that merit this Court's consideration. Ever since *Erie* was decided, the lower federal courts have had to determine the status of state law on issues where state law controls. Not infrequently, they have had to do so in circumstances where the highest state court has not spoken to the particular issue. There is no disagreement about how such a determination is to be made: the federal court may consider "all of the available legal sources" to determine "issues of state law as it believes the highest court of the state would determine them." 19 Charles A. Wright, Arthur R. Miller

& Edward H. Cooper, *Federal Practice & Procedure*, § 4507, pp. 130, 191 (1996). These decisions are generally not subject to review by this Court:

> [O]rdinarily we accept and therefore do not review, save in exceptional cases, the considered determination of questions of state law by the intermediate federal appellate courts.

Huddleston v. Dwyer, 322 U.S. 232, 237 (1944).

Contrary to the suggestion made in the Petition, the question the Fifth Circuit faced in this case had *not* been decided by *any* Texas appellate court – including the four intermediate court decisions to which SHT repeatedly cites.[10] The question was whether, under Texas law, a potential investor in a publicly-held corporation with no previous connection to either the corporation or the accountant is within a "limited group" of persons who is entitled to rely upon the auditor's report in asserting a negligent misrepresentation cause of action under section 552 of the Restatement (Second) of Torts. While other Texas cases had discussed the negligent misrepresentation cause of action, none addressed that precise question.

---

[10] In its "Reasons for Granting the Writ," SHT states that the Fifth Circuit "ignored the clear holdings of four Texas intermediate court cases on the issue of negligent misrepresentation," and that the Fifth Circuit "[failed] to abide by the holdings of the Texas courts. . . . " (Petition, p. 7) These statements are simply wrong. The Fifth Circuit correctly noted that "[t]he Texas courts have not had occasion to decide this particular aspect of the "limited group" requirement. . . . " (81 F.3d at 613)

The Fifth Circuit here did not deviate from the normal approach in making its "considered determination" of this issue under Texas law. It certainly did not "ignore" clear holdings of Texas intermediate courts, as Petitioners claim. The Fifth Circuit had before it all "available legal sources," namely, the Texas state appellate court opinions regarding Section 552 of the Restatement (Second) of Torts, which governs the tort of negligent misrepresentation in Texas, as well as the federal decisions addressing Texas negligent misrepresentation law and the Restatement itself. Because the Restatement has been adopted by many other jurisdictions in addition to Texas, it also considered other judicial decisions interpreting the Restatement. The court also had its own determination of the Restatement in *Rubinstein v. Collins*, 20 F.3d 160, 172 (5th Cir. 1994) (Texas law) and *First Nat'l Bank of Commerce v. Monco Agency Inc.*, 911 F.2d 1053, 1057-60 (5th Cir. 1990) (Louisiana law). There is absolutely nothing in the Fifth Circuit's thorough analysis that deviates from the standard and well-established judicial approach in these circumstances.

B. The Fifth Circuit's Conclusion on the Issue of Texas State Law Is Well Supported

The best indicators of how the Texas Supreme Court would address the question in this case are found in two different sources, both of which the Fifth Circuit took into account. First, the Texas Supreme Court had adopted Section 552 of the Restatement as the law of Texas with regard to negligent misrepresentation causes of action. *Federal Land Bank Ass'n v. Sloane*, 825 S.W.2d 439, 442 (Tex.

1991). The success of SHT's argument on its negligent misrepresentation claim depended on Texas law being "more expansive than the Restatement approach" to third-party liability. (81 F.3d at 612-14) However, since the time of SHT's cited appellate decisions, the Texas Supreme Court has adopted Restatement Section 552, not something different, as the law of the state. (*Id.* at 612)

Second, the closest that any of the Texas appellate courts had come to discussing the issue in this case was in *Cook Consultants v. Larson*, 700 S.W.2d 231, 236 (Tex. App. – Dallas 1985, writ ref'd n.r.e.). That case dealt with the potential liability of a surveyor to the property's purchaser, who the court found was the *only* potential user of the information. The court specifically contrasted the result in that case with an "unlimited class" of securities purchasers:

> Unlike, for example, future purchasers of shares of stock attempting to hold an accountant liable, [plaintiff] Larson is not a member of an unlimited class . . .

700 S.W.2d at 236 (citations omitted).[11]

---

[11] The Fifth Circuit made a detailed analysis of Texas law, citing to cases that gave some guidance on the question it was deciding, including two of the four cases it is accused of ignoring. (81 F.3d at 612-14) It did not cite to two of the Texas appellate decisions because they were not helpful. *Shatterproof Glass Corp. v. James*, 466 S.W.2d 873 (Tex. Civ. App. – Fort Worth 1971, writ ref'd n.r.e.), dealt with an identified party relying on financial statements in a specific transaction, all known to the auditor in advance. *Hermann Hosp. v. National Standard Ins. Co.*, 776 S.W.2d 249 (Tex. App. – Houston [1st Dist.] 1989, writ denied), involved a misrepresentation made *directly* by the

One of SHT's chief complaints is that the Fifth Circuit examined the discussion of Texas law on this same issue contained in *In re Crazy Eddie Securities Litigation*, 812 F. Supp. 338, 359-60 (E.D.N.Y. 1993). SHT argues that the Fifth Circuit "heavily relied" on that case. To the contrary, the Fifth Circuit specifically acknowledged that *In re Crazy Eddie* had no binding effect on the court. (81 F.3d at 613)

Finally, SHT's arguments are founded upon a grave misunderstanding of Texas procedure. SHT argues that the Texas Supreme Court refused writs of error in three of the four Texas cases and, thereby, adopted those opinions as its own.[12] (Petition, pp. 29-30) This argument is incorrect. The history of three of these four cases in the Texas Supreme Court was "writ refused, no reversible error." Under the Texas Supreme Court's rules, this means that the Supreme Court was not satisfied that the court of appeals' opinion correctly stated the law in all respects, but there was no error that required reversal.[13]

---

defendant insurance company to the plaintiff-hospital that a patient was insured. Liability to a third party was not even raised in *Hermann*.

[12] The means by which an appeal is taken to the Texas Supreme Court is by "application for writ of error." Texas Rules of Appellate Procedure 130. The Supreme Court's disposition of the writ, the case's "writ history," is significant under Texas procedure and therefore is noted in the citation.

[13] The fourth case, *Hermann Hospital*, was "writ denied," which meant that the Texas Supreme Court was not satisfied that the opinion declared the law correctly in all respects, but believed that reversal was not required *or* that the case was not of such importance to the state's jurisprudence as to require correction. The Appendix to this brief contains a table

(Appendix) In none of the four decisions did the Texas Supreme Court adopt the court of appeals' opinion as its own.[14]

The thrust of SHT's *Erie* argument is that it simply disagrees with the Fifth Circuit's decision, nothing more. It also makes clear that its success on the limited group argument relies very heavily on the assumption that the Texas Supreme Court would reject the Restatement and adopt an expansive "foreseeability" approach to the limited group requirement of the negligent misrepresentation cause of action. However, as the Fifth Circuit noted, one of the Texas intermediate cases "expressly declined . . . to adopt the foreseeability approach" (81 F.3d at 614) and the clear nationwide trend is to reject such an expansive test in the context of third-party liability for merely negligent misrepresentation. (81 F.3d at 611)

---

explaining the meaning of the various writ dispositions by the Texas Supreme Court.

[14] This would only be true in those cases in which the Texas Supreme Court rules on the application with the notation "writ refused." None of the four cases relied upon by SHT are cases in which the application for writ of error was simply refused. In any event, if SHT were correct and had the Texas Supreme Court adopted the three opinions as its own, it means that *Cook Consultants'* statement that "future purchasers of shares of stock attempting to hold an accountant liable" are not members of any limited group would function as a statement of the Texas Supreme Court. Finally, this case does not create an intra-circuit conflict with the procedures approved in *Comer v. Texaco, Inc.*, 514 F.2d 1243, 1244 (5th Cir. 1975). *Comer* interpreted Louisiana, not Texas, appellate procedure.

The Fifth Circuit carefully analyzed Texas law and trends in Texas law and drew its conclusion concerning what the Texas Supreme Court would decide. It is not the function of this Court to waste its resources to determine whether the Fifth Circuit was correct in its determination of what the Texas Supreme Court would do. If there were ever a situation where this Court was being asked to take a case of "isolated significance," SHT's *Erie* question is it. *See Rice v. Sioux City Memorial Park Cemetery*, 349 U.S. 70, 76 (1955).

Finally, SHT's *Erie* argument is confined to the limited group issue. The justifiable reliance aspect of the court's decision is not contested. Further, the Fifth Circuit specifically noted at the end of its opinion that, had it not decided the case in Peat Marwick's favor on negligent misrepresentation and justifiable reliance, some of the other appellate issues raised by Peat Marwick – particularly damages and loss causation – also had "considerable merit." (81 F.3d at 615) This Court should not grant petitions for certiorari when alternative holdings make the question presented to this Court too abstract. *See, e.g., The Monrosa v. Carbon Black Export, Inc.*, 359 U.S. 180, 183-84 (1958).

CONCLUSION

For the reasons stated herein, the petition for writ of certiorari should be denied.

Respectfully submitted,

MORRIS HARRELL*
Counsel of Record

TIMOTHY W. MOUNTZ
CYNTHIA KEELY TIMMS
LOCKE PURNELL RAIN HARRELL
(A Professional Corporation)
2200 Ross Avenue, Suite 2200
Dallas, Texas 75201-6776
214/740-8000

DAVID M. PYKE
RADER, CAMPBELL, FISHER & PYKE
2777 Stemmons Freeway
Stemmons Place, Suite 1080
Dallas, Texas 75207
214/630-4700

ANTHONY J. COSTANTINI
SUTHERLAND, ASBILL & BRENNAN
600 Madison Avenue, 11th Floor
New York, New York 10022
212/332-3000

Attorneys for Respondents

Dated: August 1996

APPENDIX –

**Texas Rules of Form,
Tex. Law Rev. Ass'n
(8th ed. 1992),
Appendix A**

APPENDICES

APPENDIX A
TABLE OF NOTATIONS USED ON APPLICATIONS FOR WRITS OF ERROR

(From Gordon Simpson, *Notations on Applications for Writs of Error*, 12 TEX. B.J. 547, 574-75 (1949))
[Post-1949 information added]

Notation	Date[18]	Statute or Rule Defining Notation	Meaning
Refused [writ ref'd]	Sept. 1, 1892 to June 14, 1927	None. *Cf.* Acts 1892, 1st C.S., ch. 14, p. 20; Art. 943, R.S. 1895; Art. 1544, R.S. 1911; Art. 1746, R.S. 1925.	Supreme Court approved result reached by court of civil appeals but did not necessarily approve opinion. Brackenridge v. Cobb, 85 Tex. 448, 21 S.W. 1034 (1893); Fleming v. Texas Loan Agency, 87 Tex. 238, 27 S.W. 126 (1894). Refusal might not even mean approval of result reached, where error was not preserved and presented to Supreme Court. See Terrell v. Middleton, 108 Tex. 14, 17, 191 S.W. 1138, 1139 (1917).
	June 14, 1927 to present	Acts 1927, Reg. Sess., ch. 144, p. 214, amending Art. 1728, R.S.	Judgment of court of civil appeals correct and principles of law declared in opinion correctly determined. Hamilton v. Empire Gas & Fuel Co., 134 Tex. 377, 383-84, 110 S.W.2d 561, 565-66 (1937); Ohler v. Trinity Portland Cement Co., 181 S.W.2d 120, 123 (Tex. Civ. App.—Galveston 1944, no writ) ("Since [June 14, 1927], a decision by a Court of Civil Appeals in which the Supreme Court refuses a writ of error[] is as binding as a decision of the Supreme Court itself.").
Refused for Want of Merit; Ref. Want Merit; Ref. W.M. [writ ref'd w.o.m.]	Sept. 1, 1941 to Feb. 1, 1946	Tex. R. Civ. P. 483.	Judgment of court of civil appeals correct but Supreme Court not satisfied that opinion in all respects has correctly declared the law.

[18]Date of Supreme Court's action on the application. See tables of cases reviewed, published in the *Texas Reports*, for exact date of action.

Notation	Date	Statute or Rule Defining Notation	Meaning
Refused, No Reversible Error; Ref. N.R.E. [writ ref'd n.r.e.]	Feb. 1, 1946 to Jan. 1, 1988	Tex. R. Civ. P. 483 (repealed 1986); TEX. R. APP. P. 133.	Supreme Court not satisfied that opinion of court of civil appeals in all respects has correctly declared the law, but is of the opinion that the application for writ of error presents no error which requires reversal.[19]
Dismissed; Dismissed for Want of Jurisdiction; dismissed WOJ [writ dism'd w.o.j.]	Sept. 1, 1892 to July 1, 1917	None. *Cf.* Acts of 1892, 1st C.S., ch. 15, § 5, p. 26; Art. 996, R.S. 1895; Art. 1591, R.S. 1911; Acts 1892, 1st C.S. ch. 14, p. 20; Art. 940, R.S. 1895; Art. 1521, R.S. 1911, and amending acts.	Lack of jurisdiction in Supreme Court to consider application. Examples: jurisdiction final in court of civil appeals, Burnett v. Powell, 86 Tex. 382, 24 S.W. 788, 25 S.W.17 (1894) (boundary suit), Gulf C.&S.F.R. Co. v. Buford, 85 Tex. 430, 21 S.W. 678 (1893) (amount in controversy), Meade v. Leon & H. Blum Land Co., 85 Tex. 513, 22 S.W. 514 (1893) (question of fact); defective application, Homes v. City of Henrietta, 91 Tex. 318, 42 S.W. 1052 (1897); application filed too late, Schleicher v. Runge, 90 Tex. 456, 39 S.W. 279 (1897); subject matter of controversy has ceased to exist, Robinson v. State, 87 Tex. 562, 29 S.W. 649 (1895); judgment of court of civil appeals not one which "practically settles the case," Gulf C.&S.F.R. Co. v. Riordan, 85 Tex. 511, 22 S.W. 514 (1892).
	July 1, 1917[20] to June 14, 1927	*Cf.* Art. 1591, R.S. 1911, and Acts 1917, Reg. Sess., ch. 75, p. 141, amending Art. 1521, R.S. 1911; Arts. 1728 and 1821, R.S. 1925.	Same as above, except extended to include cases otherwise within jurisdiction of Supreme Court where error committed, if any, was not "of such importance to the jurisprudence of the State as in the opinion of the Supreme Court required correction." Decker v. Kirlicks, 110 Tex. 90, 95-96, 216 S.W. 385, 386-87 (1919); National Compress Co. v. Hamlin, 114 Tex. 375, 385-86, 269 S.W. 1024, 1028 (1925).

[19]Prior to 1988, some commentators questioned whether the definition in Rule 483 of the "no reversible error" designation accurately or completely described its use in practice. Ted Z. Robertson & James W. Paulsen, *The Meaning (If Any) of an "N.R.E.,"* 48 TEX. B. J. 1306 (1985); *cf.* Frank M. Wilson, *Hints on Precedent Evaluation*, 24 TEX. B.J. 1037, 1089-91 (1961) (suggesting various clues to the reasons for a court's use of the *writ ref'd n.r.e.* designation in a particular case). In particular, it was suggested that the Texas Supreme Court's method of processing writ of error applications made *writ ref'd n.r.e.* a catch-all designation to which a specific interpretation—that the court was troubled by a certain aspect of the court of appeals' declaration of the law but satisfied with the disposition of the case—could not accurately be ascribed.

[20]The 1917 act provided that it should become effective on July 1, 1917, but that it should not affect business before the Supreme Court at that time. Records in the clerk's office indicate that applications filed after July 1, 1917, were not acted on by the Supreme Court until after January 1, 1919.

Notation	Date	Statute or Rules Defining Notation	Meaning
Dismissed; Dismissed for Want of Jurisdiction; Dismissed WOJ [writ dism'd w.o.j.] (continued)	June 14, 1927 to Mar. 1, 1939	Acts 1927, ch. 144, p. 214, amending Art. 1728, R.S. 1925; Art. 1821, R.S. 1925.	(1) Lack of jurisdiction in Supreme Court to consider application. See examples above. (2) In cases within jurisdiction of Supreme Court, judgment correct but Supreme Court not satisfied that opinion of court of civil appeals in all respects has correctly declared the law. Bain Peanut Co. v. Pinson & Guyger, 119 Tex. 572, 574-75, 34 S.W.2d 1090, 1091 (1931). (*Cf.* "Refused" prior to 1927.)
	Mar. 1, 1939 to present	Supreme Court Rule 5a, 131 Tex. v; Tex. R. Civ. P. 483; TEX. R. APP. P. 133.	Lack of jurisdiction in Supreme Court to consider application. See examples above. Wood v. Bankers Life & Loan Ass'n, 132 Tex. 505, 125 S.W. 2d 262 (1939).
Dismissed for Want of Jurisdiction—Correct Judgment; Dism. Judgm. Cor. [writ dism'd judgmt cor.]	Mar. 1, 1939 to Sept. 1, 1941	Supreme Court Rule 5a, 131 Tex. v.	In cases within jurisdiction of Supreme Court, judgment correct but Supreme Court not satisfied that opinion of court of civil appeals in all respects has correctly declared the law. Republic Ins. Co. v. Highland Park Indep. Sch. Dist., 133 Tex. 545, 125 S.W.2d 270 (1939).
Denied [writ denied]	Jan. 1, 1988 to present	Supreme Court Rule 133, 733 S.W.2d cxviii; TEX. R. APP. P. 133.	Supreme Court not satisfied that opinion of court of appeals in all respects has declared the law correctly, but is of the opinion that the application presents no error of law which requires reversal or which is of such importance to the jurisprudence of the state as to require correction.[21]

[21]For an explanation of the formal distinction between "writ denied" and "writ ref'd n.r.e.," and possible practical considerations, see Elaine A. Carlson & Roland Garcia, Jr., *The New Discretionary Review Powers of the Texas Supreme Court*, 50 TEX. B.J. 1201 (1987).